No. 77-1359

In the Supreme Court of the United States

OCTOBER TERM, 1977

UNITED STATES OF AMERICA, PETITIONER

v.

KIMBELL FOODS, INC., ET AL.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

The Solicitor General, on behalf of the United States of America, petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fifth Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App. A, *infra*, pp. 1A–29A) is reported at 557 F. 2d 491. The opinion of the district court (App. C, *infra*, pp. 31A–53A) is reported at 401 F. Supp. 316.

JURISDICTION

The judgment of the court of appeals (App. B, *infra*, p. 30A) was entered on August 12, 1977. A petition for rehearing was denied on October 25, 1977

(App. D, *infra*, p. 54A). On January 16, 1978, Mr. Justice Powell extended the time within which to file a petition for a writ of certiorari to and including March 24, 1978. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether a private lien that has not attached to the property and become choate before a federal lien attaches takes precedence over the federal lien.

STATEMENT

1. In February 1969 O K Super Markets, Inc., a Dallas supermarket chain, borrowed $300,000 from Republic National Bank of Dallas (App. C, *infra*, p. 34A). The Small Business Administration guaranteed 90 percent of this loan, as it is authorized to do by Section 7(a) of the Small Business Act, 72 Stat. 384, 387, as amended, 15 U.S.C. 636(a), when the "financial assistance applied for is not otherwise available on reasonable terms" from non-federal sources.[1] The financing statement executed by O K Super Markets granted the bank a security interest in all the debtor's machinery, equipment, fixtures, and inventory; the statement was filed with appropriate state officials on February 18, 1969 (App. C, *infra*, p. 34A).

O K Super Markets had executed three earlier security agreements with Kimbell Foods, Inc., in August

[1] Efforts by the bank and the Small Business Administration to have larger creditors of O K Super Markets guarantee parts of this loan had been unsuccessful (App. C, *infra*, p. 34A).

1966, April 1968, and November 1968.[2] O K received advances on inventory and gave a general security interest in the stores' equipment, fixtures, goods and merchandise (App. A, *infra*, p. 2A). Each agreement contained a standard "dragnet" clause stating that the security interest also was given to secure all future advances made by Kimbell Foods to O K Super Markets (*id.* at 3A).

By February 1969, when Republic made its federally guaranteed loan, O K Super Markets still owed Kimbell $24,893.10.[3] O K paid Kimbell using the Republic loan proceeds. In February 1969 O K also owed Kimbell $18,390.93 on open account for inventory purchases; it made payments equal to this amount, and Kimbell credited these against this balance (App. A, *infra*, pp. 3A–4A).

O K continued to make purchases on open account from Kimbell until January 15, 1971, when Kimbell filed suit in a Texas state court to recover an unpaid balance of $18,258.57 (App. A, *infra*, p. 4A). At approximately the same time, O K defaulted on its payments to Republic, which then assigned its security interest to the Small Business Administration. The agency paid the bank 90 percent of the indebtedness, which totaled $252,331.93 on that date, and filed the assignment with the proper state official (App. C, *infra*, pp. 34A–35A). Approximately a year after the

[2] The August 1966 security agreement and financing statement secured a $20,000 promissory note. The April and November 1968 security agreements and financing statements together secured a single $27,000 note (App. C, *infra*, pp. 33A–34A).

[3] O K had retired the 1966 note entirely, and the debt pertained only to the 1968 note. (App. A, *infra*, p. 3A).

assignment and filing, Kimbell obtained in a Texas state court a judgment for $24,445.37 on its claims against O K (*id.* at 33A, n. 2).

2. Kimbell filed the present suit in the United States District Court for the Northern District of Texas, seeking a declaration that its security interest in O K's property (and hence the state judgment) created a claim to O K's assets superior to that of the bank and the United States.[4] The district court held that the United States' security interest is superior (App. C, *infra,* pp. 36A–46A). It concluded that, under the governing federal law, a private lien is not entitled to priority over a federal lien unless the private lien has attached to the property, and all opportunities for contesting the amount of the lien have been exhausted, before the federal lien attaches (*id.* at 36A–42A). The court stated that because Kimbell Foods did not make its lien choate until February 1972, when the state court judgment was entered, it could not prevail over the United States' security interest, which had a priority date no later than January (*id.* at 43A).[5]

3. The court of appeals reversed. It held that the priority of the federal lien is governed by federal law,

[4] Jurisdiction was based on 28 U.S.C. 2410, relating to actions affecting property on which the United States has a lien (App. C, *infra*, p. 31A). Three of OK's stores had been sold, and Kimbell asserted a claim to the resulting funds. (*id.* at 32A–33A).

[5] The State of Texas and the City of Dallas intervened, claiming delinquent sales taxes and ad valorem taxes from the fund. The district court held that these claims did not have sufficient priority to be recognized (App. C, *infra*, pp. 46A–51A), and the intervenors did not appeal.

but it rejected the "choateness" rule followed by the district court for determining when a private lien is deemed to be perfected in competition with a federal lien. It rejected the "choateness" doctrine because it thought that the doctrine, which was developed in large part in connection with federal tax liens, should not be "extended" to situations in which the federal government is a surrogate commercial lender (App. A, *infra,* pp. 17A–19A). The court stated that the doctrine would cause potential credits of businesses that are eligible for Small Business Administration loans to shun these businesses, thereby harming the companies that the agency is supposed to assist (*id.* at 19A). It observed that Congress has altered the application of the choateness doctrine to tax liens, and argued that "logical symmetry" requires that the doctrine should not be applied to federal contractual liens (id. at 20A–22A).[6]

The court then fashioned a new federal rule for determining priorities. The court essentially adopted the Uniform Commercial Code, modified by the generally accepted federal rule that the lien "first in time is first in right" (App. A, *infra,* pp. 24A–26A).[7]

[6] The court of appeals also rejected the district court's alternate holding (App. C, *infra*, pp. 43A–46A) that Kimbell's lien could not have priority because it was not perfected under Texas law (App. A, *infra*, pp. 10A–13A). We do not present this question of state law for decision by this Court.

[7] The court of appeals subsequently decided to abandon the "first in time—first in right" rule. See *United States* v. *Crittenden*, 563 F. 2d 678 (C.A. 5). See also page 13, *infra.*

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But on the question whether the future advances clauses in the security agreements between O K and Kimbell give Kimbell's 1970 and 1971 advances a priority dating back to the 1966 and 1968 agreements, the court considered a number of rules that had been applied by other courts (*id.* at 26*a*–28*a*). It narrowed its choice to two, but found it unnecessary to choose between the rules, because either one gives Kimbell a priority dating from before the earliest possible priority for the federal lien (*id.* at 28A).

REASONS FOR GRANTING THE PETITION

1. The Small Business Administration is in charge of a national program to make or guarantee loans that private lenders find too risky. A substantial number of the borrowers are unable to repay the loans on schedule. The Small Business Administration informs us that outstanding direct loans and guarantees amount to $8 billion, and that at most times approximately $1 billion is in default or in arrears.[8] Approximately 3,400 cases are in litigation at any time, and many involve questions of priorities between federal liens and competing liens. Many of the borrowers have operations in more than one state. It is plainly desirable that there be a uniform federal rule for de-

[8] During October 1977 there were 10,853 loans involving $551,800,000 in liquidation. An additional 27,628 loans, involving $493,600,000, were delinquent.

termining the priorities of competing liens in cases involving the federal government.[9]

Uniformity has proved to be an elusive goal. The courts of appeals are divided concerning the rules for establishing priority when federal and private liens compete. At least six courts of appeals have concluded that the federal lien takes precedence unless the competing lien attached to the property and became "choate" before the attachment of the federal lien.[10] Two courts of appeals, including the court in the present case, reject the "choateness" doctrine.[11] The two

[9] The Department of Housing and Urban Development, the Veterans Administration, the Farmers Home Administration, the Economic Development Administration, and [redacted] other federal agencies also make or guarantee loans. The rules of priority affect them no less than they affect the Small Business Administration.

[10] See *Willow Creek Lumber Co., Inc.* v. *Porter County Plumbing & Heating, Inc.*, C.A. 7, No. 77–1536, decided March 16, 1978; *Chicago Title Insurance Co.* v. *Sherred Village Associates*, 568 F. 2d 217 (C.A. 1); *United States* v. *General Douglas MacArthur Senior Village, Inc.*, 470 F. 2d 675 (C.A. 2), certiorari denied *sub nom. County of Nassau* v. *United States*, 412 U.S. 922; *T. H. Rogers Lumber Co.* v. *Apel*, 468 F. 2d 14 (C.A. 10); *United States* v. *Oswald and Hess Co.*, 345 F. 2d 886 (C.A. 3); *United States* v. *Latrobe Construction Co.*, 246 F. 2d 357 (C.A. 8), certiorari denied, 355 U.S. 890. The cases from the First, Second, Seventh and Tenth Circuits were decided after Congress amended the tax lien statutes in 1966.

[11] In addition to the present case, see *United States* v. *Crittenden, supra; United States* v. *California-Oregon Plywood, Inc.*, 527 F. 2d 687 (C.A. 9); *Connecticut Mutual Life Insurance Co.* v. *Carter*, 446 F. 2d 136 (C.A. 5), certiorari denied, 404 U.S. 857; *Ault* v. *United States*, 432 F. 2d 441 (C.A. 9), affirming *Ault* v. *Harris*, 317 F. Supp. 373 (D. Alaska).

most recent appellate decisions explicitly decline to follow the decision of the court of appeals in the instant case.[12] This Court should resolve the conflict and establish a uniform rule of priority.

2. The priority of a debt due the United States "is always a federal question." *United States* v. *Security Trust & Savings Bank,* 340 U.S. 47, 49; *United States* v. *Pioneer American Insurance Co.,* 374 U.S. 84, 88–89. No federal statute governs the priority of federal liens arising from the government's lending programs, and therefore "it is for the federal courts to fashion the governing rule of law according to their own standards." *Clearfield Trust Co.* v. *United States,* 318 U.S. 363, 367.

As a starting point, federal courts have followed the "cardinal rule" that the lien "first in time is first

[12] See *Willow Creek, supra; Chicago Title Insurance Co., supra,* 568 F. 2d at 222 (footnote omitted): "What dissuades us in particular from joining the Fifth and Ninth Circuits is that we would not merely be siding with one camp, making the split in the circuits a bit more even. We would, having decided not to rely on the traditional requirement of choateness in determining the cognizable timing of a mechanic's lien, have to adopt a substitute formula. We would have difficulty in following the Fifth Circuit in *Kimbell Foods, supra,* which applied local law, the Uniform Commercial Code, to a privately held secured interest. This device fitted the case admirably, since the U.C.C. is of general, nationwide application, with no quixotic parochial variations. Recourse to the local law governing mechanics' liens, however, would incorporate many local eccentricities. This fact led the Ninth Circuit in *Ault, supra,* to adopt * * * local law [only to a degree]. Application of this rule, though, would not only require [the federal agency] to concern itself with the varying state laws, but would require contractors to be aware of the possible applicability of two sets of rules. Were we to carve out our own approach which differed from the court in *Ault,* we would have succeeded only in further complicating a minefield * * *."

in right." *United States* v. *City of New Britain,* 347 U.S. 81, 85–86; *Rankin* v. *Scott,* 12 Wheat. 177, 179. To determine which lien is "first in time," most courts have adopted the doctrine—initially developed in tax and insolvency cases (see, *e.g., County of Spokane* v. *United States,* 279 U.S. 80, 94–95 (insolvency statute);[13] *United States* v. *City of New Britain, supra* (tax lien))—that the non-federal lien has priority from the date it becomes "choate." A lien becomes choate only when "the identity of the lienor, the property subject to the lien, and the amount of the lien" have been established. *United States* v. *City of New Britain, supra,* 347 U.S. at 84. The amount of the lien usually is not established until the lien is reduced to judgment. See *United States* v. *White Bear Brewing Co., Inc.,* 350 U.S. 1010, 1011 (Douglas, J., dissenting); *United States* v. *Acri,* 348 U.S. 211.

The court of appeals concluded, however, that the choateness rule should be abolished for a variety of "policy reasons" (App. A, *infra,* p. 17A). The court's reasons, we submit, do not bear scrutiny.

a. The court of appeals observed that the choateness doctrine had been devised in tax lien cases, and it stated that the government's position as an involuntary creditor in tax cases distinguishes tax liens from other federal liens (App. A, infra, pp. 17A–18A).[14] The court also argued that it is more impor-

[13] 31 U.S.C. 191 provides that in settling the affairs of any insolvent, "the debts due to the United States shall be first satisfied."

[14] The court overlooked the fact that the choateness doctrine was developed as an application of the insolvency statute, which applies to all situations in which the government is a creditor and the debtor is an "insolvent."

tant for the government to collect taxes than to recover bad debts. It is difficult, however, to find a material distinction between a dollar received from the collection of taxes and a dollar returned to the treasury on repayment of a federal loan.

And it is not appropriate to regard the Small Business Administration as an ordinary commercial lender. Government loans, guarantees, and insurance are provided for reasons of national policy, not to make a profit. The assistance usually is provided only if commercial credit is not available on reasonable terms. 15 U.S.C. 636(a)(1); see also, *e.g.*, 7 U.S.C. 1922(4), 1941(4) (Farmers Home Administration); 42 U.S.C. 3142(b)(4) (Economic Development Administration). The court of appeals was quite wrong in reasoning that the government should be treated as an ordinary commercial lender because it "enters the commercial credit scheme" with the same "opportunity to evaluate the credit risks" as a private lender (App. A, ~~supra~~ *infra*, p. 18A). The government enters only where private lenders do not go, and the choateness rule provides appropriate protection for loans where the government is the lender of last resort.

b. The court of appeals stated (App. A, *infra,* p. 19A) that the choateness doctrine harms small businesses, the intended beneficiaries of federal assistance, because it would lead private creditors to shun businesses that could be eligible for federal loans. But the Small Business Administration's operations in jurisdictions that follow the choateness doctrine afford an opportunity to test the court's assertion; that agency

informs us that it has not detected the hesitance that the court feared. Cf. *Small Business Administration* v. *McClellan,* 364 U.S. 446, 453. The federal guarantee often substantially improves the situation of the borrower, making commercial lenders more, not less, willing to lend additional sums. In the present case, for example, the federal guarantee allowed O K to retire outstanding indebtedness and provided needed operating funds for O K's troubled business, all to the benefit of O K's creditors, who continued to advance new sums.

Moreover, an alteration in the priority rules would not be an unmixed blessing for small businesses even if, as the court of appeals speculated, the present priority rules cause some commercial lenders to treat loans to small businesses as somewhat riskier. The Small Business Administration, like other federal lending or insuring agencies, has only limited resources. It uses a revolving fund as the basis for loans and guarantees (15 U.S.C. 633(c)). Inability of the Small Business Administration to realize on the security for its loans simply reduces the amount available for future loans—to the detriment of the small businesses.

c. The suggestion that, in light of the Federal Tax Lien Act of 1966, 80 Stat. 1125, amending 26 U.S.C. 6323, "logical symmetry urges rejection of * * * the choateness doctrine" (App. A, *infra,* pp. 20A–21A), rests on a misreading of the intent of Congress. The Tax Lien Act explicity affects only tax liens, and Congress did not alter the well-understood choateness rule for any other liens. Five courts of appeals and the

Court of Claims have rejected the argument that the Tax Lien Act has any bearing on the priorities of federal non-tax liens.[15] As the court explained in *United States* v. *General Douglas MacArthur Senior Village, Inc.*, 470 F. 2d 675, 678–679 (C.A. 2), certiorari denied *sub nom. County of Nassau* v. *United States*, 412 U.S. 922 (emphasis in orginal): "[w]e are unable to conclude * * * that a Congressional enactment, carefully drawn, which affects the priority of federal *tax* liens leaves the courts free to disregard prior precedents and thus to broadly extend the scope of the statute's principle to other unspecified areas which, though somewhat analogous, were simply not addressed by the Congress."[16]

[15] *Willow Creek Lumber Co., Inc.* v. *Porter County Plumbing & Heating, Inc., supra; Chicago Title Insurance Co.* v. *Sherred Village Associates, supra; United States* v. *General Douglas MacArthur Senior Village, Inc., supra; T. H. Rogers Lumber Co.* v. *Apel, supra; H. B. Agsten & Sons, Inc.* v. *Huntington Trust & Savings Bank*, 388 F. 2d 156 (C.A. 4) (*en banc*), certiorari denied, 390 U.S. 1025; *Aetna Insurance Co.* v. *United States*, 456 F. 2d 773 (Ct. Cl.). But see *United States* v. *California-Oregon Plywood, Inc., supra.*

[16] Furthermore, the [illegible] Lien Act creates only limited exceptions to the "first in time" and choateness rules. The Act does not abolish the choateness principle even for tax liens. See H.R. Rep. No. 1884, 89th Cong., 2d Sess. 35 (1966). For example, the Act does not protect mechanics' liens that arise before the lienors provide services or materials, even if these would be protected under state law against later arising liens. 26 U.S.C. 6323(h)(2); Plumb, *Federal Tax Liens* 152 (3d ed. 1972). And the Act gives priority to future advances pursuant to a written commercial financing agreement only if they are made within 45 days of the filing of the tax lien. 26 U.S.C. 6323(c). A court could achieve "logical symmetry" only by adopting the rules of the Tax Lien Act for use in all non-tax lien cases, not by abolishing the choateness doctrine. If the court had adopted the Tax Lien Act here, it probably could not have reached the result it did, because it appears that at least some of the advances by Kimbell were made more than 45 days after the federal lien attached and therefore would not have been accorded priority in tax cases.

3. Any attempt to develop new priority rules by litigation rather than by legislation is bound to produce considerable uncertainty. Once the choateness rule had been discarded, the present case raised two difficult issues—how a private lien is perfected, and whether future advances relate back to the original agreement. The court of appeals in resolving these questions here, and in deciding *United States* v. *Crittenden*, 563 F. 2d 678 (C.A. 5), considered the Uniform Commercial Code rule, state-modified versions of the U.C.C., state rules that pre-dated the U.C.C., the English rule, and the tax lien statute. The court narrowed the field in this case, but did not select a rule for future cases. *Crittenden* even rejected the "first in time" doctrine in order to recognize a "super-priority" for repairmen's liens; super-priority claims raise questions that defy logical analysis. As the First Circuit put the matter in *Chicago Title Insurance Co.* v. *Sherred Village Associates*, 568 F. 2d 217, in the course of rejecting the approach of the present case: "[w]e cannot avoid feeling that there is much that we do not know about the equities, effects of various rules, and relative ability of the federal and local lienors to protect themselves," and new rules "could be more equitably and intelligently made after Congressional hearings, rather than after a trial between a limited number of litigants". (568 F. 2d at 221 and n. 6).[17]

[17] See also note 12, *supra.*

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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MARCH 1978.

APPENDIX A

United States Court of Appeals Fifth Circuit

KIMBELL FOODS, INC., F/K/A KIMBELL MILLING COMPANY, D/B/A KIMBELL GROCERY COMPANY, PLAINTIFFS-APPELLANTS,

v.

REPUBLIC NATIONAL BANK OF DALLAS AND UNITED STATES OF AMERICA, DEFENDANTS-APPELLEES.

No. 75-4105

Aug. 12, 1977

Rehearing and Rehearing En Banc Denied Oct. 25, 1977

A. L. Vickers, Vernon O. Teofan, Holt W. Guysi, Dallas, Tex., for plaintiffs-appellants.

Frank J. Betancourt, Dallas, Tex., for Republic Nat'l Bank.

Michael P. Carnes, U.S. Atty., Fort Worth, Tex., Charles D. Cabaniss, Asst. U.S. Atty., Dallas, Tex., for defendants-appellees.

Appeal from the United States District Court for the Northern District of Texas.

Before THORNBERRY and GEE, Circuit Judges, and MARKEY,* Chief Judge.

GEE, Circuit Judge:

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*Of the United States Court of Customs and Patent Appeals, sitting by designation.

On this appeal we must decide which creditor of a mercantile chain enjoys priority to repayment from the proceeds of the sale of assets of three supermarkets, aggregating $86,672. One of these is the Small Business Administration (hereinafter SBA), an avatar of the United States, serving as the guarantor of a private loan to the debtor. SBA claims the special priority enjoyed by the sovereign in collecting taxes and the debts owed it by insolvents. We conclude that the SBA lacks priority under either state or federal law.

The other parties are the debtor, O.K. Supermarkets, Inc. (hereinafter O.K.), and a private lender, Kimbell Foods, Inc. (hereinafter Kimbell). O.K. is a Dallas supermarket chain. The bulk sale of fixtures, equipment and inventory of three of its stores forms the fund to which the parties seek priority. O.K. owed Kimbell because of weekly inventory sales to O.K. on open account. Much of the factual background from which the claims of the parties emerged is undisputed.

O.K. executed three security agreements and financing statements to Kimbell. The first was in August 1966, securing a $20,000 promissory note from Kimbell. The collateral listed included supermarket equipment and fixtures and "[a]ll goods, wares and merchandise and any and all additions or accessions thereto." In April and November of 1968, O.K. executed the remaining security agreements and financing statements to secure a $27,000 promissory note from Kimbell. The collateral for these two agreements was again specifically identified equipment normally used in a supermarket and "[a]ll goods, wares, merchandise and stock in trade and accessions." Each of the security agreements was duly

filed, and no termination statement was filed on any of the agreements. It is of particular importance to this case that each of the security agreements included the provision that "said security interest also being given to secure the payment of all other indebtedness at any time hereafter owing by Debtor to Secured Party as well as the discharge of all obligations imposed upon Debtor hereunder."

On February 2, 1969, O.K. borrowed $300,000 from Republic National Bank of Dallas (hereinafter Republic). The SBA guaranteed 90% of this loan. On February 18, 1969, Republic filed with the Secretary of State of the State of Texas a security agreement and financing statement executed by O.K. to Republic granting it a security interest in all of the debtor's machinery, fixtures, equipment, inventory and all additions and accessions thereto.[1] When O.K. defaulted on this note the SBA paid Republic 90% of the outstanding indebtedness, some $252,313.93, and on January 21, 1971, Republic assigned the SBA 90% of the note and financing statement.

Events subsequent to the 1969 loan of $300,000 form perhaps the most important part of this tableau. When Republic made its loan, O.K. owed Kimbell $24,893.10 on the 1968 note for $27,000. O.K. paid off this note from the Republic loan proceeds. Thus, both the 1966 note[2] and the 1968 note between O.K. and Kimbell

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[1] Republic had previously filed a financing statement on August 7, 1968, covering the same collateral but refiled the statement on February 18, 1969. The district court apparently considered only the February 18 filing effective, see 401 F. Supp. at 323, as do we.

[2] The record is unclear on the disposition of the 1966 note. We may assume that it was satisfied because the parties stipulated that on February 12, 1969, the 1968 note was the only outstanding promisory note between O.K. and Kimbell.

had been satisfied. O.K. still, however, owed Kimbell $18,390.93 on open account for inventory purchases. After February 12, 1969, O.K. paid Kimbell $18,390.93 against that debt—payments Kimbell credited to O.K.'s oldest outstanding balances. O.K. kept on making inventory purchases from Kimbell on open account until January 15, 1971. By then the balance of O.K.'s account with Kimbell was $18,258.57. On January 15, 1971, Kimbell filed suit in Texas courts to recover that amount and, on January 31, 1972, obtained a judgment for $24,445.37—$18,258.57 principal, $1,186.80 interest and $5,000 attorney's fees.

Both the SBA and Kimbell claimed priority in the $86,672 proceeds of the sale of three O.K. Supermarkets. After hearing the evidence and considering the stipulations of the parties the court ruled that the SBA had priority superior to all inchoate liens by virtue of its special status as a federal lien creditor. The district court ruled Kimbell's lien inchoate because Kimbell had not reduced its lien to judgment before the SBA guaranteed Republic's note or before the SBA made good on its guarantee. The court went on to rule that Kimbell did not have a good security interest in the goods sold at bulk sale, a fact that certainly rendered its lien inchoate. Kimbell appeals.

Kimbell's Lien

We must first determine whether the district court properly held that Kimbell's security agreements securing the 1966 and 1968 notes did not cover the advances Kimbel made to O.K. on open account.[3] The

[3] Kimbell contends this question is not before the court because of stipulations in the pretrial order of the parties, who stipulated the existence of the 1966 and 1968 loans, security agreements and financing statements. Nowhere in the stipulations did the parties agree that the security agreements secured Kimbell's advances to O.K. of inventory on open account. Nor was the question explicitly listed as one of the contested issues of law in the pretrial order. The question was raised implicitly, however, in contested issues of fact and law concerning the understanding of Republic as to the priority of its lien, the effect of O.K.'s payoff of the 1968 note, and the effect of O.K.'s payments to Kimbell of amounts greater than the balance on open account outstanding just prior to Republic's 1969 loan to Kimbell. We think the question was before the court.

security agreements provide that the security interest also secures the payment of future indebtedness between the parties. Texas law countenances such so-called "dragnet clauses." *See* Tex. Bus. & Com. Code § 9.204(e) (Tex. U.C.C.).[4] Acknowledging this apparent approval of future advance clauses, the district court ruled that the future advance clause did not operate in this case. It relied on pre-Code Texas cases and U.C.C. cases from other jurisdictions to restrict the application of the future advance clause to future debts clearly contemplated by the parties. So reasoning, it ruled that in this case the parties meant the security agreements to cover only the notes for which

[4] Obligations covered by a security agreement may include future advances or other value whether or not the advances or value are given pursuant to commitment. * * * Tex.Bus. & Com. Code § 9.204(e) (1968) (Tex.U.C.C.). The Texas Business and Commerce Code, containing Texas' version of the U.C.C., was amended in 1973. The amendments changed portions of the U.C.C. relevant to this case, but those changes did not become effective until January 1, 1974. Unless otherwise noted, we rely on the Texas U.C.C. as it existed at the time of the relevant events in this case.

they were executed, not later purchases on open account. We view the transactions differently.[5]

Although the district court correctly stated the law of Texas, it arrived at the wrong conclusion in light of Texas' application of its law. Texas courts do not recognize the application of a future advance clause unless the future advance to be secured was "reasonably within the contemplation of the parties to the mortgage at the time it was made." *Wood* v. *Parker Square State Bank,* 400 S.W. 2d 898, 901 (Tex. 1966). *See also Moss* v. *Hipp,* 387 S.W. 2d 656 (Tex. 1965); Wallenstein & St. Claire, *Annual Survey of Texas Law—Property,* 30 Southwestern L.J. 28, 53 n. 214 (1976).[6] Consistent with this view, in Texas a future advance clause in a mortgage does not secure a subsequent debt from the debtor to a third party acquired from the third party by the mortgagee. *See Wood, supra.* In circumstances similar to those at bar, however, Texas courts have hinted that future advance clauses will be effective. In *Wood,* for example, the Texas Supreme Court remarked that:

> The more reasonable construction of this general language [a future advance clause] is that it referred to obligations directly arising between Lincoln Enterprises [the original debtor] and respondent bank [the original lender], i.e., where Lincoln became obligated to the bank as the maker of an obligation, or became liable in a secondary capacity in favor of the bank.

[5] The interpretation of a contract is a question of law, so we are not restricted by the clearly erroneous rule of Fed. R. Civ. P. 52(a). *See Backar* v. *Western States Producing Co.,* 547 F. 2d 876, 880 (5th Cir. 1977); *First Nat'l Bank* v. *Ins. Co. of North America,* 495 F. 2d 519, 522 (5th Cir. 1974).

[6] In the absence of Texas cases dealing with future advance clauses under the Code, we, like the district court, have drawn upon Texas' treatment of future advance clauses in other instruments. Because the Texas U.C.C. gives no indication that future advance clauses are to be treated differently today than under Texas pre-Code law, we consider the pre-Code cases dealing with other types of security interests authoritative.

Supra at 902. *See also Estes* v. *Republic National Bank,* 462 S.W. 2d 273 (Tex. 1970); Wallenstein & St. Claire, *supra* at 53 n. 214. In light of this evidence we conclude that in Texas a further extension of credit to the debtor by the lender is deemed future indebtedness reasonably contemplated by the parties when they execute a future advance clause.

The district court concluded that the parties did not intend the future advance clause to cover purchases on open account because the security agreements were intended to cover only the amounts loaned under a promissory note. In reaching this conclusion, however, the district court ignored two important factors: the parol evidence rule and Texas' treatment of future advance clauses in analogous situations. The district court admitted testimony by Harold Kindle, the president of O.K., about the subjective intention of the parties when they executed the 1966 and 1968 notes, security agreements and financing statements. Although his testimony was equivocal,[7]

[7] Indeed, well-nigh incoherent. When asked whether O.K. intended that the security agreements cover all other advances and open accounts between it and Kimbell, Kindle answered: "Well, I considered the 1966 agreement a thing of the past from the 1968 agreement. I felt like it was, you know, a new beginning and since we intended to pay the full amount—I realize it was a demand note and they could demand it at any time they wanted to, but we had had a good relationship so it was of no real concern. I didn't stop and ponder about, well, should I do this or should we do this.—O.K. Supermarkets."

When asked again, Kindle responded: "There again, there was not any specific instruction—on this question I mean—about

the district court understood him to say that the parties intended each transaction to be separate and distinct. Admisssion of such testimony was error. The language of the contract, unless ambiguous, represents the intention of the parties. The intent deduced from this objective matter, not the parties' subjective understandings, is controlling. *See Western Oil Fields, Inc.* v. *Pennzoil United, Inc.*, 421 F. 2d 387, 390 (5th Cir. 1970); *City of Pinehurst* v. *Spooner Addition Water Co.*, 432 S.W. 2d 515, 518 (Tex. 1968); *Wall* v. *Lower Colorado River Authority*, 536 S.W. 2d 688, 691 (Tex. Civ. App.—Austin 1976, writ ref'd n.r.e.). *See also First National Bank* v. *Rozelle*, 493 F. 2d 1196, 1201 (10th Cir. 1974). Testimony as to O.K.'s subjective intent in receiving the future advance clause was a classic violation of the parole evidence rule and clearly inadmissible.

The district court compounded this error by failing to consider the truest test of the parties' intention, the words of the contract clearly providing that the security agreement should cover future indebtedness. In *Estes* v. *Republic National Bank*, 462 S.W. 2d 273 (Tex. 1970), the Texas Supreme Court upheld the applicability of a future advance clause despite the debtor's claim of an oral agreement that the deed of trust containing the future advance clause was intended as a separate transaction not to extend to other

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which agreement would cover which. I felt like we signed a new statement in '68, and everything that had transpired in the past was history. I felt like that any monies expended on either one of those without an abrupt halt and then a start over again would be—that '66 would be history now and then when the '68 was paid off, it would be history as well."

indebtedness between the parties. In the absence of some evidence that the "dragnet clause" was placed in the contract by mutual mistake, the court found that the clause clearly and unequivocally stated the intention of the parties for the land to secure the debtor's other loans from the bank. *See also Wood, supra.* In light of the *Estes* and *Wood* cases, the district court improperly discarded these future advance clauses.

The district court also relied on the circumstances surrounding the 1966 and 1968 loans in finding that the parties treated each loan as a separate and distinct agreement for a specific, nonrecurring purpose and to determine that the later inventory purchases were unrelated. Examining the documents and the circumstances surrounding their execution, we find nothing that negates the parties' statement that the security agreements cover the inventory purchases on account.

The 1966 promissory note was entered into to free O.K.'s current cash flow to purchase fixtures for a new store and to allow O.K. to buy opening inventory from Kimbell on credit. At least in part, then, the 1966 security agreement contemplated the purchase of inventory on credit. The security agreement states that it is given "to secure an advance of goods, wares and merchandise and does not include a pree..isting debt." Under these circumstances we cannot say that later inventory purchases on credit by O.K. were "unrelated" to the 1966 security agreement or involved future advances "not of the same class" so as to negate the applicability of the future advance clause, as the district court held. *See* 401 F. Supp. at 325–26.

Again in 1968, O.K.'s promissory note allowed it to delay payment on its open-account purchases so as

to free current cash flow to pay off a debt owed Associated Grocers, Inc. The 1968 security agreement and financing statements were again related to Kimbell's inventory advances on open account to O.K.[8] Although the notes, security agreements and financing statements were executed in response to special factual circumstances, those circumstances are not necessarily inconsistent with giving the future advance clauses in those agreements their plain meaning, *see First National Bank* v. *Rozelle, supra* at 1201, holding that Kimbell's 1966 and 1968 security agreements and financing statements covered its later advances of inventory to O.K. on open account.

Priority Under State Law

We now consider whether Kimbell had priority under state law. If it did not, we need not consider the more pressing questions of the applicability of federal law and the relative priority of federal liens. *See United States* v. *P. S. Hotel Corp.*, 527 F. 2d 500, 501 (8th Cir. 1975). As the assignee of Republic's 1969 note and security agreement, the SBA may assert whatever priority that note might command under state law. The district court did not directly address the question of Republic's priority *qua* noteholder because of its view that Kimbell's security agreements with O.K. did not secure future advances. We find that they did, but even so the security agreement of February 18, 1969, between Republic and O.K. might be thought prior for two reasons. First, Republic may have established a security interest superior to that of Kimbell. Second, the 1969 note might be thought prior to secured future advances made after February 18, 1969. After reviewing the Texas law, we conclude that neither of these theories accords the SBA, standing in the shoes of Republic, priority in the proceeds from the bulk sale.

[8] O.K.'s failure to demand a termination statement under Tex. Bus. & Com.Code § 9.404(a) (1968) (Tex.U.C.C.) after paying off the 1968 note also tends to discredit the claim that the security agreements applied only to the 1966 and 1968 notes.

Republic could obtain a superior security interest in the collateral, notwithstanding Kimbell's previously filed security agreement, if Republic attained a purchase money security interest in the collateral. The Uniform Commercial Code, adopted in Texas, provides that a purchase-money security interest in collateral except inventory has priority over a conflicting security interest in the same collateral if the purchase money security interest is properly perfected. Tex. Bus. & Com. Code § 9.314(d) (1968) (Tex. U.C.C.). Unfortunately for Republic and the SBA, the record reflects no purchase of goods by O.K. with the proceeds of the $300,000 note that could give rise to a purchase-money security interest in any items sold at the bulk sale—except inventory.

O.K. used some of the funds from the $300,000 note to purchase inventory. Texas law affords Republic a purchase-money security interest in that inventory and grants Republic priority: *if* the security interest was perfected at the time the debtor received possession; *if* the holder of the purchase-money security interest notified the holders of prior security interests before the debtor received possession of the collateral; and *if* that notice stated that the person giving notice had or expected to acquire a purchase-money security interest in the specifically described goods. Tex. Bus. & Com. Code § 9.312(c) (1968) (Tex. U.C.C.). Republic did not give the required notice to Kimbell so

as to establish priority in the inventory. *See Borg Warner Acceptance Corp.* v. *Wolfe City National Bank,* 544 S.W. 2d 947, 951 (Tex. Civ. App.—Dallas 1976, no writ). Kimbell was vaguely aware that Republic was planning to loan O.K. funds and would expect to acquire a lien, but Republic never gave Kimbell the notification requisite for priority under the Code. Republic never notified Kimbell that it expected to acquire a lien on the inventory, nor did it describe the inventory by item or type. Republic thus forfeited whatever priority it could have attained. Republic had priority, therefore, only if its lien was prior in time to Kimbell's.

Here we again inquire into the nature of the future advance clause and the security interest it creates, a particularly important endeavor when, as here, the inquiry determines the status of the lien of an intervening secured creditor. The Texas U.C.C. provides in § 9.312(e)(1) that the first filed of conflicting security interests perfected by filing prevails. Tex.Bus. & Com.Code § 9.312(e)(1) (1968) (Tex.U.C.C.). In this case both Kimbell's and Republic's security interests were perfected by filing; Kimbell would normally have priority unless the future advance did not qualify because of the creation of an intervening security interest. The circumstance of a future advance after an intervening filed security interest does not alter the scheme, however. When both the interests are filed security interests, we interpret section 9.312 (e) of the U.C.C. to adopt the relation-back position so that the first-to-file rule awards priority even to an advance made after an intervening security interest. *See* Tex. Bus. & Com. Code § 9.312(e)(1) and Example 4 (1968) (Tex. U.C.C.); Cohen, *The Future Advance Interest Under the Uniform Commercial*

Code: Validity and Priority, 10 B.C. Ind. & Com. L. Rev. 1, 13 (1968); Comment, *Priority of Future Advances Lending Under the Uniform Commercial Code,* 35 U. Chi. L. Rev. 128, 133–34 (1967). The 1972 amendments to the U.C.C., adopted by Texas in 1973, effective in 1974, explicitly adopted the relation-back position for future advances. *See* Tex. Bus. & Com. Code § 9.312(g) (Supp.1976) (Tex.U.C.C.). Although no Texas cases confirmed the prior U.C.C. provisions' adoption of the relation-back doctrine, the doctrine was consistently upheld in pre-Code Texas cases involving future advances. *See Freiberg v. Magale,* 70 Tex. 116, 7 S.W. 684, 685 (1888); *Crabb v. William Cameron & Co.,* 63 S.W.2d 367, 368 (Tex. Com.App.1933, judgm't adopted); *Coke Lumber & Mfg. Co. v. First National Bank,* 529 S.W. 2d 612, 615 (Tex. Civ.App.—Dallas 1975, writ ref'd). *See also* Wallenstein & St. Claire, *supra* at 53–54 n. 214. Under Texas law, Kimbell retained a superior lien to Republic, and the SBA, as Republic's assignee, held an inferior state lien.

Priority Under Federal Law

The SBA asserts that, despite its poor showing under state law, under federal law it has a claim superior to Kimbell's.[9] The SBA asserts the federal

[9] We have recently ruled that federal law controls the rights and duties of the United States when it operates the SBA loan program. *United States* v. *Terrey,* 554 F. 2d 685 (5th Cir. 1977). *See Miree* v. *DeKalb County,* —— U.S. ——, 97 S. Ct. 2490, 53 L. Ed. 2d 557 (1977); *Clearfield Trust Co.* v. *United States,* 318 U.S. 363, 63 S. Ct. 573, 87 L. Ed. 838 (1943). One matter in the record suggests that this principle may not apply. The February 18, 1969, security agreement between Republic and O.K. provided

common law priority rule of "first in time, first in right" and the peculiar patina that federal courts have placed on that rule specifying that only "choate" nonfederal liens may qualify as "first in time." We conclude that the "choateness" rule of federal common law does not apply here.

Understanding the SBA's argument requires a review of the development of the federal common law of priority. The source of much of federal priority law is the congressional declaration awarding the United States priority for the payment of its debts from certain insolvents.[10] In 31 U.S.C. § 191 (1970) (or Revised

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that "This agreement shall be construed according to the laws of the State of Texas." The agreement bound the parties' assigns to this provision; thus, the SBA was bound to the application of Texas law in its pursuit of its rights against O.K. *See United States* v. *Whitehouse Plastics*, 501 F. 2d 692, 694 n. 1 (5th Cir. 1974). *Cf. United States* v. *Terrey*, 554 F. 2d 685 (5th Cir. 1977). *But see United States* v. *Outriggers, Inc.*, 549 F. 2d 337, 340 n. 5 (5th Cir. 1977) (SBA regulation requires application of federal law to SBA documents). Nevertheless, we cannot read the language in the security agreement as waiving the SBA's right to have federal law applied in evaluating the priority of its interest against those of third parties.

[10] Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts, makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed, or absent debtor are attached by process of law, as to cases in which an act of bankruptcy is committed.
31 U.S.C. § 191 (1970). Although our present concept of governmental priority developed as an intrinsic privilege of the English crown, the United States' priority derives solely from statute. *See*

Statutes § 3466 as it is more commonly known), Congress requires that in settling the affairs of certain insolvents "the debts due to the United States shall be first satisfied." Section 3466 had been read as only granting the United States, as an unsecured creditor, a priority against other unsecured creditors, *see* Kennedy, *The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien*, 63 Yale L. J. 905, 909–11 (1954), thus recognizing the integrity of pre-exisiting liens. But in *Spokane County* v. *United States*, 279 U.S. 80, 49 S. Ct. 321, 73 L. Ed. 621 (1929), the Supreme Court concluded that the priority granted the United States would defer only to specific and perfected ("choate") liens prior in time. 279 U.S. at 93–95, 49 S. Ct. 321. To further protect the United States' priority under section 3466, the Supreme Court ruled that whether a lien was choate involved a matter of federal law, *see United States* v. *Waddill, Holland & Flinn, Inc.*, 323 U.S. 353, 65 S. Ct. 304, 89 L. Ed. 294 (1945), thus preventing states from divesting the United States of priority by adopting their own definitions of what constituted a choate state lien. Later the Supreme Court narrowly defined what could qualify as a choate lien,[11] effectively assuring absolute priority to United States claims under section 3466. *See* Plumb, *Federal Liens and Priorities—Agenda for the Next Decade*, 77 Yale

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United States v. *Vermont*, 377 U.S. 351, 358, 84 S. Ct. 1267, 12 L. Ed. 2d 370 (1965); *United States* v. *New Britain*, 347 U.S. 81, 84, 74 S. Ct. 367, 98 L. Ed. 520 (1954).

[11] To assure that his lien was choate, the private lien holder must establish the identity of the lienor, the property subject to the lien, and the fixed amount of the lien. *See, e.g., United States* v. *New Britain*, 347 U.S. 81, 74 S. Ct. 367, 98 L. Ed. 520 (1954);

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L. J. 228, 230 (1967); Kennedy, *From Spokane County to Vermont: The Campaign of the Federal Government Against the Inchoate Lien,* 50 Iowa L. Rev. 724, 736 (1965); Burroughs, *The Choate Lien Doctrine,* 1963 Duke L. J. 449, 452. *See generally,* Lacy, *Effect of Federal Priority and Tax Lien Legislation on Creditors of Vendors and Purchasers,* 50 Ore. L. Rev. 621, 625–31 (1971). Our case does not require the application of section 3466, since O.K. is not an insolvent, but the SBA invokes the choateness doctrine spawned by section 3466 to claim priority.

The SBA bases its argument on judicial extension of the choateness doctrine to determine priority for other federal liens. Although the federal tax statute accorded the United States a lien for taxes only—making no mention of priority for federal tax liens, *see* 26 U.S.C. § 6321 (1970)—in *United States v. Security Trust & Savings Bank,* 340 U.S. 47, 71 S. Ct. 111, 95 L. Ed. 53 (1950), the Supreme Court held that the choateness principles of section 3466 were equally applicable when a federal tax lien was competing for priority with a state lien. The purpose of the tax lien statute was to assure prompt and certain collection of taxes from tax delinquents; this purpose required a rule similar to that prevailing with collections under section 3466, 340 U.S. at 51, 71 S. Ct. 111. Other federal courts, without questioning

United States v. *Pioneer American Ins. Co.*, 374 U.S. 84, 83 S. Ct. 1651, 10 L. Ed. 2d 770 (1963). Because the amount of the lien was not fixed until the lienor had exhausted his opportunities to challenge the amount, the Court indicated that only possession or reduction to judgment would meet the last criterion. *See, e.g., United States* v. *Gilbert Associates, Inc.*, 345 U.S. 361, 73 S. Ct. 701, 97 L. Ed. 1071 (1953). *See also Texas Oil & Gas Corp.* v. *United States*, 466 F. 2d 1040, 1044–45 (5th Cir. 1972).

whether the reasons for extending the choateness doctrine of section 3466 to tax liens justified its extension to other liens, have applied the doctrine to bestow overriding priority on other federal liens. ***See, e. g.,*** *T. H. Rogers Lumber Co v. Apel,* 468 F. 2d 14 (10th Cir. 1972) (FHA mortgage lien); *United States v. Oswald & Hess Co.,* 345 F. 2d 886 (3d Cir. 1965) (SBA mortgage lien); *In re Lehigh Valley Mills, Inc.,* 341 F. 2d 398 (3d Cir. 1965) (SBA security interest). *See also,* Plumb, *Federal Liens & Priorities—Agenda for the Next Decade,* 77 Yale L. J. 228, 286–87 (1967). The SBA asks us to accord it this superior status in this ordinary commerical transaction far removed from the doctrine's origins by arguing that the choateness doctrine is an inevitable consequence of applying federal law; but as our study reveals, the choateness concept is a judicial creation distinguishable from the well-recognized federal rule of "first in time, first in right." *See Texas Oil & Gas Corp. v. United States,* 466 F. 2d 1040, 1045 (5th Cir. 1972); Plumb, *supra* at 230. History in this area does not permit us to enshrine without analysis the status sought by the SBA. Viewing the choateness doctrine independently, strong policy reasons militate against its application in this context.

First, the interests supporting the Supreme Court's extension of section 3466's criteria to tax liens in *Security Trust* do not support a similar extension to liens arising from SBA garden-variety commercial loans or guaranties. The choateness doctrine reflects a judicial recognition of the self-preservation prerogative of the sovereign. Taxes are its lifeblood, and the choateness doctrine recognizes and protects that vital flow. Delinquent taxes make the United States an involuntary creditor of the taxpayer, often ranged

against other substantial commercial creditors and state tax creditors. By the time the United States becomes aware of its status and files its tax lien, it may well—absent self-help—find itself standing at the end of the state priority line. The Supreme Court's extension of the choateness doctrine protected the collection of taxes and gave the United States, a sovereign, a measure of relief from its involuntary-creditor status. When the United States, however, in its less-exalted capacity as SBA, serves as a surrogate commercial lender or guarantor, it enters the commercial credit scheme voluntarily. These circumstances afford it an opportunity to evaluate the credit risks, to examine the interests of other creditors, and to exact such security as the circumstances and policy of the program dictate. *See* Plumb, *The Relative Priority of Federal and Business Claims: Yesterday, Today and Tomorrow*, 27 Bus. Lawyer 1195, 1217 (1972); Comment, *The Priority of Federal Claims: Selected Problems and Theoretical Considerations*, 24 Case W. L. Rev. 521, 534–35 (1973); Comment, *The Relative Priority of SBA Liens: An Unreasonable Extension of the Federal Preference*, 64 Mich. L. Rev. 1107, 1128–29 (1966). As a quasi-commercial lender, SBA (U.S.A.) does not require, and should not be accorded, the special priority which it compels as sovereign, so long as it complies with Congress' admonition that it make loans which are "of such sound value or so secured as reasonably to assure repayment." 15 U.S.C. § 636(a)(7) (1970). *See* Comment, *The Relative Priority of SBA Liens: An Unreasonable Extension of the Federal Preference, supra* at 1119.

Second, in a related concern, the importance of taxes to the functioning of government mer-

its the extraordinary priority accorded them by the judge-made "choateness" doctrine. The Supreme Court has long recognized that section 3466 is informed by the importance of securing adequate revenue to sustain the public burdens and discharge the public debts. *See United States* v. *Moore*, 423 U.S. 77, 81–82, 96 S. Ct. 310, 46 L. Ed. 2d 219 (1975); *United States v. Emory*, 314 U.S. 423, 426, 62 S. Ct. 317, 86 L. Ed. 315 (1943); *United States* v. *State Bank of North Carolina*, 6 Pet. 29, 35, 8 L. Ed. 308, 310 (1832). Consequently it has transferred that respect for revenue-protecting measures to the tax-lien statute. *See Security Trust, supra.* On the other hand, the SBA program is a supplement to commercial loan operations, certainly less central to the proper functioning of the national government and less deserving of the extraordinary priority accorded by the choateness doctrine.

Third, granting the SBA an exceptional priority pursuant to the choateness doctrine is inconsistent with the congressional declaration of policy pursuant to its establishment of the SBA. In 15 U.S.C. § 631 (1970), Congress declares that the purpose of the SBA assistance program is "to assist in the establishment, preservation, and strengthening of small business concerns * * *." If the SBA may belatedly buy into loans and so assert liens superior to those of prior secured creditors, every sane potential creditor of small business will shun potential debtors of the SBA as anathema or extract promises that the debtor will not seek SBA assistance. What secured creditor will extend credit on collateral that may only serve to increase the security of a future SBA loan? Such a legal posture scarcely assures a steady flow of capital into necessitous small business.

Finally, logical symmetry urges rejection of the SBA's effort to extend the choateness doctrine to this context. The primary thrust of the SBA's argument is that because section 3466's choateness doctrine was extended to tax liens it should be extended to SBA contractual liens. Yet in the Federal Tax Lien Act of 1966 Congress substantially pared the applicability of the choateness doctrine by recognizing that certain state lien interests, including security interests, could attain priority over tax liens. *See* 26 U.S.C. § 6323 (1970). *See generally,* Coogan, *The Effect of the Federal Tax Lien Act of 1966 Upon Security Interests Created Under the Uniform Commercial Code,* 81 Harv. L. Rev. 1369 (1968). Why should the choateness doctrine bestow priority on an SBA contractual lien when a United States tax lien, more in need of the protection of the choateness doctrine, commands no such priority? *Connecticut Mutual Life Ins. Co.* v. *Carter,* 446 F. 2d 136, 139 (5th Cir.), *cert. denied,* 404 U.S. 857, 92 S.Ct. 104, 30 L. Ed. 2d 98 (1971); *Ault* v. *Harris,* 317 F. Supp. 373, 375 (D. Alaska), *aff'd and opinion adopted,* 432 F. 2d 441 (9th Cir. 1970). *See* Note, 3 Rutgers Camden L. Rev. 592, 597 (1972).[12] In the absence of any congressional directive to extend the choateness doctrine[13] and in our role as judicial custodians of the doctrine, we decline to extend it further in this Circuit.

[12] The district court distinguished *Connecticut Mutual's* analogy to the 1966 Tax Lien Act by relying on cases in other circuits and a subsequent case in our circuit reaffirming the existence of the choateness doctrine. 401 F. Supp. at 323–24. In *Texas Oil & Gas Corp.* v. *United States,* 466 F. 2d 1040 (5th Cir. 1972), we utilized the choateness doctrine to adjudge whether a state lien fitted the priority provisions of the 1966 Tax Lien Act. This action is not inconsistent with our refusal to extend the choateness doctrine to SBA security interests because previous case law had established the applicability of the choateness doctrine to statutorily-created federal tax liens. The 1966 Tax Lien Act adjusted the application of the doctrine by recognizing the priority of certain state interests, essentially granting exceptions to the choateness doctrine. In this area of SBA contractual liens, the choateness doctrine has not been established as a concomitant to the application of the federal "first in time, first in right" rule. We consider the 1966 Tax Lien Act as neither affirming nor denying the applicability of the choateness doctrine to other federal liens, but the Act's recognition that some state claims should have priority over federal tax liens is a strong policy argument against extending the choateness doctrine to deny priority to state claims. Accordingly, the decisions of other circuit courts that deny that the 1966 Tax Lien Act was intended to subordinate other federal liens are consistent with our approach. *See T. H. Rogers Lumber Co.* v. *Apel,* 468 F. 2d 14 (10th Cir. 1972); *United States* v. *General Douglas MacArthur Senior Village, Inc.,* 470 F. 2d 675 (2d Cir. 1972). We differ with those courts because, unlike them, we do not consider the choateness doctrine a necessary companion to the federal "first in time, first in right" priority scheme.

[13] In 15 U.S.C. § 646 (1970), Congress subordinates SBA interests in property to state property taxes: "Any interest held by the Administration in property, as security for a loan, shall be subordinate to any lien on such property for taxes due on the property to a state, a political subdivision thereof, in any case when such lien would, under applicable state law, be superior to such interest if such interest were held by any party other than the United States."

This statute could be read as ameliorating the impact of the choateness doctrine by waiving the immunity it would grant, thus implicitly recognizing the applicability of the choateness doctrine to SBA liens. We have read the enactment less broadly, noting that the purpose of § 646 is to waive the extraordinary priority of § 3466, 31 U.S.C. § 191 (1970). *See City of Sherman* v. *United States,* 400 F. 2d 373, 377 (5th Cir. 1968). By giving SBA liens the same status as state liens with regard to state tax claims, the provision also has the effect of waiving the "first in time, first in right" principle to recognize the state's grant of priority to later liens for state and local taxes. *See Edmondson* v. *Chesapeke*

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The SBA argues that circuit courts have already concluded that the choateness doctrine applies to mortgage liens, so it should apply here in the virtually identical situation of a federal contractual lien competing against state liens. It is true that a number of courts, including ours, have concluded that the federal "first in time, first in right" approach to priority applies to federal mortgage liens. *See United States v. Roessling,* 280 F. 2d 933 (5th Cir. 1960) (mortgage lien under Emergency Relief Appropriation Act of 1935); *United States v. General Douglas MacArthur Senior Village,* 470 F. 2d 675 (2d Cir. 1972) (HUD mortgage lien); *Director of Revenue v. United States,* 392 F. 2d 307 (10th Cir. 1968) (SBA mortgage lien); *United States v. County of Iowa,* 295 F. 2d 257 (7th Cir. 1961) (Reconstruction Finance Corp. mortgage lien); *Southwest Engine Co. v. United States,* 275 F. 2d 106) (10th Cir. 1960) (SBA chattel mortgage lien). Those cases are not necessarily authority for adoption of the choateness doctrine here, however, for in each case the application of the "first in time, first in right" doctrine, *without using the concept of choateness,* could have given priority to the federal liens because each competing state lien arose after the federal lien. *See Roessling, supra* at 935; *General Douglas MacArthur Senior Village, supra* at 677; *Director of Revenue, supra* at 313; *County of Iowa, supra* at 257–58; *Southwest Engine Co., supra* at 107. *See also,* Plumb, *Federal Tax*

Clamchip Corp., 350 F. Supp. 1236, 1239 (D. Md. 1972). In light of these purposes we detect no implicit congressional recognition of and reaction to the general application of the choateness doctrine.

Liens & Priorities—Agenda for the Next Decade, 77 Yale L. J. 228, 287 n. 368 (1967); Comment, *The Relative Priority of SBA Liens: An Unreasonable Extension of the Federal Preference,* 64 Mich. L. Rev. 1107, 1128 (1966). Only the Third Circuit has applied the choateness doctrine to give priority to federal contractual liens when an unvarnished "first in time, first in right" approach would have given priority to the state claims. *See United States v. Oswald & Hess Co.,* 345 F. 2d 886 (3d Cir. 1965) (SBA mortgage lien); *In re Lehigh Valley Mills, Inc.,* 341 F. 2d 398 (3d Cir. 1965) (SBA mortgage lien). But there the Third Circuit assumed without analysis that "choateness" was part and parcel of the federal law. Our examination of the history of the choateness doctrine and the policy arguments against its extension to circumstances when the United States acts as lender persuade us to reject the Third Circuit's approach and hold that the choateness doctrine does not apply to give priority to the SBA's contractual lien in the absence of insolvency.[14]

[14] Even if we did apply the choateness doctrine to this claim, it is not certain that the SBA's lien would prevail. To be choate, the identity of the lienor, the property subject to the lien, and the amount of the lien must be established. *See* note 10, *supra.* For state liens competing with federal tax liens or liens with § 3466 priority, the last requirement meant that the lienor must have either obtained a judgment or the lien must have been enforceable by summary proceeding. *See United States* v. *Acri,* 348 U.S. 211, 214, 75 S. Ct. 239, 99 L. Ed. 264 (1955); *United States* v. *Liverpool & London & Globe Ins. Co.,* 348 U.S. 215, 217, 75 S. Ct. 244, 99 L. Ed. 268 (1955). Under these criteria, federal liens with § 3466 priority are virtually invulnerable to state claims. Kennedy, *From Spokane County to Vermont: The Campaign of the Federal Government Against the Inchoate Lien,* 50 Iowa L. Rev. 724, 736 (1965). The Supreme Court intimated

Despite our decision that the choateness doctrine alone does not give the SBA priority, the question the choateness doctrine addresses still remains: how does a federal court determine when a state lien has arisen so that it may decide whether the state or the federal lien is "first in time?" Whatever the answer to that question may be in other contexts,[15] in the con-

prior to the 1966 Tax Lien Act, however, that the choateness criteria might be more easily satisfied by state liens competing against federal tax liens because Congress had not provided priority for tax liens. *See United States* v. *Vermont*, 377 U.S. 351, 385, 84 S. Ct. 1267, 12 L. Ed. 2d 370 (1964); *Crest Finance Co.* v. *United States*, 368 U.S. 347, 82 S. Ct. 384, 7 L. Ed. 2d 342 (1961); *Texas Oil & Gas Corp.* v. *United States*, 466 F. 2d 1040, 1045–46 (5th Cir. 1972). *See also* Coogan, *The Effect of the Federal Tax Lien Act of 1966 Upon Security Interests Created Under the Uniform Commercial Code*, 81 Harv. L. Rev. 1369, 1378–79 (1968); Kennedy, *supra* at 737; Burroughs, *supra* at 465–69. Similarly, Congress has not provided priority for SBA liens in noninsolvency cases: relaxation of the stringent choateness requirements also appears proper. Further, the same reasons that argue against the extension of the choateness doctrine to federal contractual liens would urge us to adopt a less stringent standard of choateness in this context.

Thus, Kimbell's lien could qualify as "choate." The 1966 and 1968 security agreements and financing statements provided the identity of the lienor and the property subject to the lien. Although Kimbell had not fixed the amount of its lien by reducing it to judgment before the SBA lien arose on January 21, 1971, *see infra*, it had terminated extensions of credit so that its accounts reflected the final amount of the claim secured by its security agreements with O.K. This could suffice to meet relaxed criteria applied to liens competing with federal contractual liens. *Cf. Crest Finance Co.*, *supra* (credit or secured by assignment of accounts receivable with perfected lien under state law had choate lien as against federal tax lien). *See also* Burroughs, *supra*, at 470.

[15] Other types of state liens—for taxes, for mechanics and materialmen, or for certain types of secured loans—present problems

text of competing state security interests arising under the U.C.C., we conclude that liens perfected under the UCC qualify to compete against federal liens under the federal "first in time, first in right" priority rules.[16] The UCC carefully prescribes the steps necessary to perfect a security interest. Perfection under the UCC provides many of the assurances of the existence of a lien required by the choateness doctrine—identity of the debtor, identity of the lienholder, and identity of the property serving as collateral. Further, the UCC embodies rules of nationwide applicability—all states but Louisiana have adopted it—assuring that federal contractual liens will not be subject to the idiosyncracies of particular state laws. *Cf. First National Bank v. SBA,* 429 F. 2d 280, 286 (5th Cir. 1970). The context provides our final reason: perfection under the UCC provides protection to the secured creditor against later-filed claims of other creditors; in

that we leave for another day. First, the manner of perfection of those liens is diverse—creating havoc with a nationwide program—and may not provide notice sufficient for federal entities to ascertain their existence before granting loans. Second, consideration of these loans for qualification under the federal "first in time, first in right" rule is complicated by the fact that several states, including Texas, either provide special priority for the liens, see *e.g.*, Tex.Tax.—Gen.Ann. art. 1.07(1) (1969) (preferred lien for state and city taxes), or allow subsequently perfected liens to relate back to the date the debt was incurred. See, *e.g.*, Tex.Rev.Civ.Stat.Ann. art. 5459 § 2(a) (Supp. 1976) (mechanic's liens have priority from date construction commences).

[16] In reaching our conclusion we do not apply state law—for we have previously concluded that federal law controls here—but we rather adopt portions of state law in order to fashion a proper federal rule. See *United States* v. *Terrey*, 554 F. 2d 685, 692 (5th Cir. 1977); *Ault* v. *Harris*, 317 F. Supp. 373, 376 (D. Alaska), *aff'd and opinion adopted*, 432 F. 2d 441 (9th Cir. 1970).

the absence of congressional mandate or persuasive policy reasons to the contrary, it should similarly protect secured creditors against later arising federal contractual liens.

Even given our conclusions that the choateness doctrine does not apply here and that perfection under the UCC will qualify a lien as "first in time," Kimbell must still establish that its lien was "first in time" under federal law. Its task is complicated because, although Kimbell had a perfected lien on the collateral, the indebtedness the lien secured results from future advances made after Republic made its loan to O.K. When the SBA bought into Republic's loan in 1971, it bought Republic's lien and for purposes of federal priority under "first in time, first in right," the SBA's lien "attached" when Republic's lien arose in 1969. *See United States v. Ekland,* 369 F. Supp. 1052, 1054–55 (S.D.Ill.1972). Under Texas law, as we have seen, the lien securing future advances dates from Kimbell's prior security interest. Does Kimbell's lien retain that date under federal common law and thus remain prior in time to the Republic-SBA lien?

Perhaps because of the pervasiveness of the choateness doctrine, we have found no federal case discussing the substantive content of the "first in time, first in right" rule with regard to future advances. Faced with the necessity of fashioning a federal common-law rule because of congressional silence on the subject, *see Clearfield Trust Co. v. United States* 318 U.S. 363, 376, 63 S. Ct. 573, 87 L. Ed. 838 (1943), we grapple with the problem by first examining the approach taken by the states.

Prior to the Uniform Commercial Code, the states adopted diverse rules on whether an optional (as opposed to an obligatory) future advance would relate back to take priority from the date of the

original security agreement. The majority rule was that optional advances made before the advancing creditor received actual notice of an intervening lien related back to the date of the original security interest. *See* Cohen, *The Future Advance Interest Under the UCC: Validity & Priority,* 10 B. C. Ind. & Comm. L. Rev. 1, 12 (1968); 59 C. J. S. *Mortgages* § 230(1)(1949); 55 Am. Jur. 2d *Mortgages* § 352 (1971). A minority of jurisdictions adopted what was known as the *Michigan* rule in which, although the prior lien was effective to secure the future advance, the lien was effective only from the date the future advance was made. Intervening encumbrances took priority over subsequent future advances. Cohen, *supra* at 12–13. Another minority view, based on older English precedent, held that optional future advances related back regardless of actual notice of intervening liens "for it was the Folly of the second Mortgagee, with Notice, to take such security." *Gordon v. Graham,* 22 Eng. Rep. 502, 2 Eq. Ca. Abr. 598 (1716). *See* Cohen, *supra* at 11. As we have seen, the ubiquitous U.C.C., at least with respect to competing security interests perfected by filing, adopted the third rule. *See, e.g.,* Tex. Bus. & Com. Code § 9.312 (e)(1) (1968) (Tex.U.C.C.).

Our brief survey of American jurisprudence evidences at least this: the trend of thought in American law rejects the *Michigan* rule and allows future advances secured by an earlier security agreement to take priority from the date of the earlier security agreement under some circumstances. We believe that federal common law should recognize this legal principle.[17] *Cf. United States v. State of Alabama,* 313

[17] The existence of various legal rules on future advances reflects the underlying conceptual problem of future advances. One

U.S. 274, 61 S. Ct. 1011, 85 L. Ed. 1327 (1941) (inchoate tax lien that became choate after United States purchased property gave due notice of liability and, when amount of tax was certain, related back to day lien imposed). Given that, however, we need go no further in crafting federal common law for this case [18] because under either the actual notice rule or the U.C.C. rule Kimbell's lien related back to its prior security agreement and was prior in time to the SBA's lien.

Kimbell's future advances relate back to and have the priority of its original security agreements with O.K. because at the time of the future advances Kimbell had no notice of the SBA's lien. Thus, under the stricter "actual notice" rule for relation back, Kimbell had no notice of the SBA's intervening interest. It is true that Kimbell was aware of Republic's lien and—so the record suggests—the SBA's guaranty of

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view is that a security interest that provides for optional future advances creates a single lien when the interest is perfected. Further future advances may increase the amount that the lien secured, but the security interest itself is one and indivisible. A second view is that a security interest for optional future advances may complete most of the requisities of perfection and give notice of possible future advances but that a future advance under the agreement takes a discrete lien dating from the day of the advance. Comment, *Priority of Future Advances Lending Under the Uniform Commercial Code*, 35 U. Chi. L. Rev. 128, 136–38 (1967). The original U.C.C. weighed heavily in favor of the single interest theory, *see e.g.*, Tex. Bus. & Com. Code § 9.312 (e)(1) & Example 4 (1968) (Tex. U.C.C.), and the 1972 amendments endorse the single interest theory more strongly. *See, e.g.*, Tex. Bus. & Com. Code § 9.312(g) (Supp. 1976) (Tex. U.C.C.).

[18] Strong policy arguments favoring greater protection for the SBA counsel adoption of the actual notice rule while equally strong considerations—similar to the ones that argue against the choateness rule—urge adoption of the U.C.C. rule. We reserve the final resolution of this difficult decision for another day.

the loan the lien secured.[19] Yet under Texas law—the U.C.C.—this notice could not affect Kimbell's decision whether to advance funds because under state law its advances were secured by and took the priority of the 1966 and 1968 security agreements. It was only when the SBA bought into the note in February 1971 that Kimbell could have actual notice of the existence of a federal lien and the application of federal law. At oral argument the United States conceded that before it bought into Republic's note it had no lien. Without actual notice of another lien that could supersede the priority of its future advances under state law, Kimbell's advancements are secured by and take the priority of the 1966 and 1968 security agreements.

In summary, the SBA's purchase of 90% of Republic's loan to O.K. vested it with Republic's lien, and, in measuring priority under federal law, the SBA's lien attached when Republic's lien arose in 1969. All of Kimbell's future advances were made subsequent to Republic's loan, but the future advances are secured by the 1966 and 1968 security agreements and take priority from those dates. Thus, Kimbell's lien for inventory advances is prior in time to the SBA's lien, and Kimbell has priority in the proceeds from the sale of the three O.K. Supermarkets.

REVERSED.

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[19] Kimbell's awareness of the SBA's guaranty did not suffice as actual notice that the SBA had a lien. At oral argument the United States admitted that it had no lien until Republic assigned its lien on January 21, 1971.

See *Lakeshore Apartments, Inc.* v. *United States*, 351 F. 2d 349, 353 (9th Cir. 1965); *City of New York* v. *United States*, 414 F. Supp. 90, 92 (E.D.N.H. 1975). *Cf. United States* v. *Marxen*, 307 U.S. 200, 205, 59 S. Ct. 811, 83 L. Ed. 1222 (1939) (United States as guarantor not a creditor in bankruptcy when note assigned it after petition filed); *In re Miller*, 105 F. 2d 926, 928–29 (2d Cir. 1939).

APPENDIX B

United States Court of Appeals for the Fifth Circuit

No. 75-4105

D. C. Docket No. CA 3-74-56 D

KIMBELL FOODS, INC., F/K/A KIMBELL MILLING COMPANY, D/B/A KIMBELL GROCERY COMPANY, PLAINTIFFS-APPELLANTS

v.

REPUBLIC NATIONAL BANK OF DALLAS AND UNITED STATES OF AMERICA, DEFENDANTS-APPELLEES

Appeal from the United States District Court for the Northern District of Texas

Before THORNBERRY and GEE, *Circuit Judges,* and MARKEY,[1] Chief Judge

JUDGMENT

This cause came on to be heard on the transcript of the record from the United States District Court for the Northern District of Texas, and was argued by counsel;

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, reversed;

It is further ordered that defendants-appellees pay to plaintiffs-appellants, the costs on appeal to be taxed by the Clerk of this Court.

August 12, 1977.

Issued as Mandate: November 2, 1977.

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[1] Of the United States Court of Customs and Patent Appeals, sitting by designation.

APPENDIX C

In the United States District Court for the Northern District of Texas, Dallas Division

(Civil Action No. 3-74-56-D)

(Filed September 8, 1975)

KIMBELL FOODS, INC., A CORPORATION, F/K/A KIMBELL MILLING COMPANY, D/B/A KIMBELL GROCERY COMPANY, PLAINTIFF,

v.

REPUBLIC NATIONAL BANK OF DALLAS AND UNITED STATES OF AMERICA, DEFENDANTS, AND STATE OF TEXAS AND CITY OF DALLAS, INTERVENORS

MEMORANDUM OPINION

This suit concerns the relative priorities of various parties to $86,672.00, which is being held in escrow by Republic National Bank. Jurisdiction is based upon Title 28, United States Code, Section 2410, this suit being brought to quiet title and foreclose liens upon personal property in which the United States claims an interest.

It will be necessary to cover each of the conflicting claims in greater detail later, however, a brief rendition of the facts might be helpful at this point. The claim of the plaintiff, Kimbell Foods, stems from weekly inventory purchases made on open account by O.K. Super Markets, Inc., a supermarket chain that operated in Dallas, Texas. Kimbell Foods claims that this indebtedness was secured by future advance

clauses in security agreements executed by O.K. Super Markets in 1966 and 1968. The Republic Bank and the United States claim entitlement to the entire proceeds in escrow due to a default by O.K. Super Markets on a $300,000.00 Small Business Administration guaranteed loan made by Republic National Bank in February of 1969. Intervenors State of Texas and the City of Dallas are seeking sums owed by O.K. Super Markets for delinquent sales taxes. Additionally, the City of Dallas is asserting a small claim for delinquent ad valorem taxes on O.K. Super Markets' personal property.

As noted previously, all of these parties are asserting claims against funds being held in escrow by Republic National Bank. The source of these funds was a bulk sale of all the fixtures, equipment and inventory at three of O.K. Super Markets' stores. These stores were purchased on February 8, 1971, by Grand City Groceries, Inc., Pat H. Hood and Charles W. Logan.[1] The stores were sold pursuant to an agreement entered into on February 3, 1971, between O.K. Super Markets and the Republic National Bank and approved as to form and substance by the Small Business Administration and Kimbell Foods. This agreement was the result of a meeting held on December 30, 1970, between a representative from the bank, the acting Regional Director of the Small Business Administration (hereinafter referred to as the SBA) and Mr. Harold Kindle, the President of O.K. Super Markets. This agreement allowed O.K. Super Markets to find bulk purchasers for the stores and in return the bank released the debtor to the extent of $95,000.00 owing on the $300,000.00 note. The agreement further provided that the bank would hold the total sum in escrow pending voluntary settlement or court adjudication of the claims of the SBA, Republic Bank and Kimbell Foods.

[1] Grand City Groceries purchased the collateral located at 3026 Grand Avenue in Dallas for $30,000.00, which represented $18,000.00 for inventory and $12,000.00 for fixtures, equipment and other property. The O.K. Super Market collateral located at 3805 Kiest Boulevard in Dallas was sold to Pat Hood for the same price as the above. Charles Logan bought the collateral at 1903 South Ervay in Dallas for $35,000.00, $21,000.00 being attributable to inventory and $14,000.00 for fixtures, equipment and other property.

Kimbell Foods contends that its claim for $24,445.37[2] is first and prior to the other claims of the parties herein. O.K. Super Markets executed three security agreements and financing statements in favor of Kimbell Foods to secure the payment of certain notes. The first of these agreements was executed on August 30, 1966, to secure a note in the sum of $20,000.00 and it was duly filed with the Secretary of State on September 2, 1966. The list of collateral which was attached to the agreement consisted of various types of equipment that would be needed in the operation of food stores. The agreement had a standard printed "dragnet" clause which said that the security interest in the listed collateral was also given to secure all other future advances to the debtor.[3] Subsequently, on April 17, 1968, and November 14, 1968, additional security agreements and fi-

[2] On February 4, 1972, Kimbell Foods obtained a judgment against O.K. Super Markets and others in the 96th Judicial District Court of Tarrant County, Texas, in the sum of $18,258.57 principal, $1,186.80 interest and $5,000.00 in attorney's fees.

[3] The August 4, 1966 agreement provided as follows: * * * "said security interest also being given to secure the payment of all other indebtedness at any time hereafter owing by Debtor to Secured Party as well as the discharge of all obligations imposed upon Debtor hereunder."

nancing statements were entered into between O.K. Super Markets and the plaintiff, securing a note in the sum of $27,000.00. These were both filed with the Secretary of State. New collateral was listed in each of these agreements and each contained an identical future advance clause as the 1966 security agreement and financing statement. These future advance clauses are said by Kimbell Foods to encompass the later inventory purchases on open account and, therefore, the security interest in the inventory is perfected as of the first filing in 1966. No termination statements have been filed on any of these security agreements.

The United States is involved in this case due to the fact that the SBA guaranteed 90% of a $300,000.00 loan made by Republic National Bank to O. K. Super Markets on February 12, 1969. This loan was sought and was needed by O.K. Super Markets because consumer boycotts at some of their stores caused heavy losses. Prior to this loan, the bank and the SBA tried to get some of the larger creditors of O.K. Super Markets to guarantee the loan in proportion to the amount owed each creditor by O.K. Super Markets but this effort proved to be unsuccessful.

To secure this $300,000.00 note O.K. Super Markets executed a security agreement and financing statement in favor of Republic Bank, which provided that the bank would have a security interest in all of the debtor's machinery, fixtures, equipment and inventory. A financing statement had been previously filed with the Secretary of State on August 7, 1968, but the financing statement was refiled on February 18, 1969, following the making of the loan.

Even with this boost, the financial difficulties of O.K. Super Markets continued, and they defaulted on the note with the bank. Therefore, the United

States on February 3, 1971, paid Republic National Bank 90% of the outstanding indebtedness, which totaled $252,331.93 on that date. The note and the financing statement were assigned to the SBA and the assignment was filed with Secretary of State on January 21, 1971.

When the SBA guaranteed loan was made by Republic National Bank on February 12, 1969, there was a balance owing on the April 17, 1968, note between O.K. Super Markets and Kimbell Foods in the sum of $24,893.10. This was the only outstanding note balance remaining on that date, however, there was a running balance on the open account for inventory purchases. Out of the $300,000.00 loaned to O.K. Super Markets, $24,893.10 was immediately paid to the plaintiff on February 12, 1969, thereby extinguishing the last remaining promissory note balance.

The claim of the State of Texas and the City of Dallas is principally for sales taxes that were due and payable by O.K. Super Markets when they sold the stores to Charles Logan, Pat Hood and Grand City Groceries. The State is seeking $29,887.51 in taxes, penalties and interest, and the City of Dallas claims $12,229.64. The intervenors contend that under State law they have a preferred lien which is first and prior to all others on all property purchased from O.K. Super Markets. They further contend that their liens follow the proceeds in escrow received from the sale of the stores.

Although recordation was not required until January 1, 1970, for a valid tax lien on personalty, the State did record its tax liens prior to that date. After this suit was filed, the State and City obtained a default judgment in the District Court of Travis

County, Texas, on February 13, 1973, against O.K. Super Markets for past due taxes.

Aside from these sales taxes, the City of Dallas claims $2,530.10 for delinquent ad valorem personal property taxes, penalties and interest for the years 1969 through 1972. These ad valorem tax liens have not been recorded nor has a judgment been obtained thereon.

The above is a summary of the claims of each of the parties. The Court will now discuss the law applicable to this case.

The initial inquiry for this Court is whether state or federal law or a combination of both controls the disposition of these conflicting claims. Jurisdiction is based upon a federal statute, 28 U.S.C.A. §2410, and it has long been the rule that federal law applies when a debt owing the United States is involved. *United States* v. *Security Trust & Savings Bank*, 340 U.S. 47 (1950); *Clearfield Trust Company* v. *United States*, 318 U. S. 363 (1943); *United States* v. *General Douglas MacArthur Sr. Vil., Inc.*, 470 F. 2d 675 (2d Cir. 1972); *Texas Oil & Gas Corporation* v. *United States*, 466 F. 2d 1040 (5th Cir. 1972); *United States* v. *City of Albuquerque, New Mexico*, 465 F. 2d 776 (10th Cir. 1972); *United States* v. *Oswald and Hess Company*, 345 F. 2d 886 (3d Cir. 1965); *In re Lehigh Valley Mills, Inc.*, 341 F. 2d 398 (3d Cir. 1965); *W. T. Jones and Company* v. *Foodco Realty, Inc.*, 318 F. 2d 881 (4th Cir. 1963). The reason for this rule is that the United States, in exercising its governmental functions must be protected by a uniform federal law and should not be subjected to differing rules of the various states. *Clearfield Trust Co.* v. *United States*, supra. Therefore, federal law applies to a consideration of all the claims in this case, unless of course there is a

federal statute directing this Court to apply state law. See Annot. 17 A.L.R. Fed. 874 (1973).

The federal rule for determining the relative priority between a federal lien and a state created lien is first in time is first in right. *United States* v. *New Britain*, 347 U.S. 81 (1954). In applying this rule, the Supreme Court has consistently held that for a non-federal lien to be entitled to priority it must be both earlier in time and be choate at the time the federal lien arises. *United States* v. *New Britain*, supra; *United States* v. *Waddill Company*, 323 U.S. 353 (1945); *United States* v. *Pioneer American Ins. Company*, 374 U.S. 84 (1963). A non-federal lien meets the choateness test only if the identity of the lienor, the property subject to the lien, and the amount of the lien are established. *United States* v. *New Britain*, supra at 84; *United States* v. *Pioneer American Ins. Company*, supra at 89; *United States* v. *General Douglas MacArthur Sr. Vil., Inc.*, supra at 678. The last requirement that the amount of the lien be certain is only established if there is no further opportunity for contesting the amount of the lien. Thus, the lienor must have either obtained a judgment or the lien must be enforceable by summary proceeding. *United States* v. *Acri*, 348 U.S. 211 (1955); *United States* v. *Liverpool & London Ins. Company*, 348 U.S. 215 (1955); *In re Lehigh Valley Mills, Inc.*, supra. With few exceptions no common law, equitable, or statutory lien can meet the federal standard of choateness unless the lienor's claim has been reduced to judgment. Plumb, *Federal Liens and Priorities—Agenda for the Next Decade*, 77 Yale L. J. 228, 230 (1967).

It has been said that the interim steps of filing and recording a private or statutory lien, without obtain-

ing a final judgment enforcing the lien against the property serves "merely as a caveat of a more perfect lien to come."[4] *United States* v. *Vorreiter,* 355 U.S. 15 (1957) (prior recorded mechanics' lien); *United States* v. *Hulley,* 358 U.S. 66 (1958) (prior recorded materialman's lien). Thus, in *United States* v. *White Bear Brewing Company,* 350 U.S. 1010 (1956), a federal tax lien was held entitled to priority over a state mechanic's lien, even though the mechanics' lien was specific under state law, it had been recorded for a certain amount, and suit had been instituted *before* the federal tax lien arose. The law that has developed around federal tax liens has been consistently applied to federal mortgage liens. *United States* v. *General Douglas MacArthur Sr. Vil., Inc.,* supra (HUD mortgage lien); *T. H. Rogers Lumber Company* v. *Apel,* 468 F. 2d 14 (10th Cir. 1972) (FHA mortgage lien); *In re Lehigh Valley Mills, Inc.,* supra (SBA mortgage lien).

Further, there is authority for the proposition that a private or statutory state lien cannot be considered choate unless it has attached to certain property *by reducing it to possession* on the theory that the United States has no claim against property no longer in the possession of the debtor. *United States* v. *Gilbert Associates,* 345 U.S. 361, 366 (1953); *W. T. Jones and Company* v. *Foodco Realty, Inc.,* supra at 887.

Although a state may characterize a lien as choate and specific, this is not conclusive, and this determination is always subject to reexamination by a federal court. *United States* v. *New Britain,* supra; *Illinois* v. *Campbell,* 329 U.S. 362 (1946); *Texas Oil & Gas*

[4] Justice Cardozo first used this expression in *New York* v. *Maclay,* 288 U.S. 290, 294 (1933).

Corporation v. *United States,* supra at 1050. Thus, the Fifth Circuit, in the *Texas Oil & Gas* case stated:

> * * * In the instant case, it is true that the bank had done all it could do under the Uniform Commercial Code to secure its interest in taxpayor-debtor's accounts receivable. However, that conclusion simply does not answer the case law as it has developed in the area of tax liens. However "complete" a lender's perfection may be under state recording laws and however "specific" state law might deem that interest to be, it is federal law that determines the extent to which that state determination will protect a private lien from a Federal tax lien. 466 F. 2d at 1051.

Of course, if the state itself would characterize a lien as inchoate, then that determination would be almost conclusive. *Illinois* v. *Campbell,* supra.

From these cases, it is clear that the plaintiff and the intervenors must show that their liens attached and were perfected under the law of Texas *and* were choate under federal law prior to the time the SBA lien became choate. *Texas Oil & Gas Corporation* v. *United States,* supra at 1052. The participation of the SBA in the Republic Bank loan was evident from the face of the note, therefore, their lien would be perfected as of the time of the February 18, 1969, filing. The SBA's claim to priority would be unaffected by the fact that formal assignment by the bank did not occur until approximately a year later. See *Director of Revenue, State of Colorado* v. *United States,* 392 F. 2d 307 (10th Cir. 1968); *W. T. Jones and Company* v. *Foodco Realty, Inc.,* supra; *Texas Oil & Gas Corporation* v. *United States,* supra.

The continued validity of the federal choate lien test was questioned by two decisions which construed the effect of the Federal Tax Lien Act of 1966 (P.L. 89–719, 80 Stat. 1125), on federal tax and mortgage liens. See *Ault* v. *Harris,* 317 F. Supp. 373 (D. Alaska 1968), aff'd per curiam (by adoption) 432 F. 2d 441 (9th Cir. 1970); *Connecticut Mutual Life Insurance Company* v. *Carter,* 446 F. 2d 136 (5th Cir. 1971). In *Connecticut Mutual* an inchoate lien for attorney's fees contained in a first mortgage was entitled to priority over a FHA mortgage lien where the FHA expressly took their second mortgage subject to first mortgage. Over a strong dissent by Judge Rives, the Court held that:

> * * * the statute [Federal Tax Lien Act of 1966] diminishes the validity of the choate lien test in the important field of taxation where the doctrine originated. It would indeed be anomalous and contrary to our view of congressional intent to allow the FHA operating as a money-lending agency to prevail in a situation where the government as holder of a tax lien would have an inferior security interest. 446 F. 2d at 139.[5]

The rationale of the *Ault* and *Connecticut Mutual* cases seems to be that since Congress chose to subordinate federal tax liens in certain specified instances that they intended to subordinate all other federal liens. However, at the same time these courts recognized that Congress had spoken only to tax liens, and

[5] The *Connecticut Mutual* decision prompted one District Court to remark that, "The prognosis for the choate lien test is guarded following the decision in Connecticut Mutual Life Insurance Co. v. Carter, * * *." *Nova Univ. of Advanced Tech., Inc.* v. *Motor Vessel Gypsy,* 331 F. Supp. 721, 722 (S.D. Fla. 1971).

other federal liens were not specifically covered by the statute.

This rationale has been questioned by two later decisions of the Second and the Tenth Circuit Courts of Appeal. In *T. H. Rogers Lumber Company* v. *Apel,* supra, the Court in construing the priorities between a FHA mortgage lien and mechanics' and materialman's liens stated:

> The fact that Congress chose to subordinate tax liens furnishes no evidence that it intended to subordinate all other federal liens to interests created by the laws of the individual states. The 1966 Act applied only to tax debts, and the reports of the House and the Senate speak only of subordinating federal unrecorded tax liens to mechanics' liens. There is not the slightest indication of the intent of Congress to subordinate other claims. 468 F. 2d at 18.

The Second Circuit in *United States* v. *General Douglas MacArthur Sr. Vil., Inc.,* supra, also concurred with the view of the Tenth Circuit:

> We are unable to conclude, however, that a Congressional enactment, carefully drawn, which affects the priority of federal *tax* liens leaves the courts free to disregard prior precedents and thus to broadly extend the scope of the statute's principle to other unspecified areas which, though somewhat analogous, were simply not addressed by the Congress. Although Judge Weinstein's carefully considered opinion forcefully argues that such an extension represents the best balancing of competing interests, his discussion would more appropriately be addressed to Congress. But where Congress has considered proposals of a highly qualified committee and has enacted

> specific, carefully-tailored legislation, it would be inappropriate for a court to undertake piecemeal extensions of the principles reflected in this legislation merely because it is desirable, especially in view of the fact that Congress saw fit not to provide for these extensions. * * * In view of the national scope of the problem and the absence of legislation extending the priority of property tax liens beyond the confines of the federal tax lien, the rule of first in time, first in right, followed by the Supreme Court, must apply. 470 F. 2d at 678–679.[6]

Additionally, the Fifth Circuit has now dispelled any thought that the federal choate lien test was abolished by the *Connecticut Mutual* case. In *Texas Oil & Gas Corporation* v. *United States,* supra, the Court stated that:

> * * * It does not appear to this Court that the 1966 amendments to the tax lien statutes did away with the choateness doctrine of United States v. Security Trust, *supra.* The Supreme Court expressly rejected that inference after earlier amendments to the tax lien statutes. *See* United States v. Pioneer American, supra. 466 F. 2d at 1053.

Therefore, this Court concludes that the federal choate lien test is still applicable to the claims of the parties herein and the *Connecticut Mutual* case is limited to the particular set of circumstances with which that Court was faced. The Court will now examine the claims of the parties with the law previously discussed as a foundation.

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[6] See also, *H. B. Agsten & Sons, Inc.* v. *Huntington Trust & Savings Bank*, 388 F. 2d 156 (4th Cir. 1967); *Aetna Insurance Co.* v. *United States*, 456 F. 2d 773 (Ct. Cl. 1972).

As noted previously, the plaintiff's claim is for purchases made by O.K. Super Markets for inventory sold on an open account. The claim of Kimbell Foods, and the parties have so stipulated, represents charges for goods sold to O.K. Super Markets subsequent to the date the SBA guaranteed loan was made on February 12, 1969, and the Court determines that these charges were also subsequent to the February 18th filing of the financing statement.

Although the Court has found that the SBA security interest attached and was perfected in February of 1969, this is not of primary importance in the consideration of the plaintiff's cause of action vis-a-vis that of the United States. Because even if the government lien was not choate until the filing of the assignment on January 21, 1971, the Court would still have to conclude that the claim of the United States would be prior in time. The elements for a private choate lien are that the identity of the lienor, the property subject to the lien and the *amount* of the lien be certain. As previously discussed, the last requirement is satisfied only when there is no further opportunity to judicially challenge the amount of the lien. This occurred when Kimbell Foods reduced its lien to judgment on February 4, 1972, some two years after the SBA guaranteed loan was made to O.K. Super Markets and more than one year after the assignment was filed. Therefore, on this ground alone the claim of the United States could be entitled to priority.

However, there is another and perhaps more basic reason for the subordination of the plaintiff's claim to that of the United States. Under the choate lien test, if the State of Texas would refuse to recognize

the lien as choate and valid, then that determination would be almost conclusive upon this Court. As previously stated, Kimbell Foods contends that under state law the future advance clauses found in the 1966 and 1968 security agreements and financing statements apply to and secure the purchases made by O.K. Super Markets on open account.

This Court is convinced that a Texas Court would conclude that the future advance clauses on the printed forms would not secure the later purchases on open account. Prior to the adoption of the Uniform Commercial Code, Texas courts have had occasion to construe these "dragnet clauses." These Courts stress that these provisions will apply only to future indebtedness that was clearly contemplated by the parties at the time of the making of the original agreement. When the agreement provides that the collateral secures, "all other indebtedness of any kind arising between the parties," this is construed to mean future indebtedness of the same nature as that previously described in the instrument. See *Wood* v. *Parker Square State Bank,* 400 S.W. 2d 898 (Tex. 1966); *Moss* v. *Hipp,* 387 S.W. 2d 656 (Tex. 1965); *Finger Furniture Company* v. *Chase Manhattan Bank,* 413 S.W. 2d 131 (Tex. Civ. App.—San Antonio, 1967, writ ref'd n.r.e.).

Section 9-204(e) of the Uniform Commercial Code, *Tex. Bus. & Comm. Code Ann.* § 9.204(e) (1968), allows the creation of clauses in an original security agreement that would secure future advances made to the original debtor. However, these clauses will be closely scrutinized and will be enforced only to the extent that future transactions or liabilities sought to be secured were in the clear contemplation of the parties. The reason for this rule is that this device can be

abused when a lender seeks to bring in claims against the debtor that were not originally contemplated by the parties. *John Miller Supply Co., Inc.* v. *Western State Bank,* 10 U.C.C. Rep. Ser. 1329, 55 Wis. 2d 385 (Wis. Sup. 1972). The future advances must be of the same class as the primary obligation and be so related that the consent of the debtor may be inferred. 2 Gilmore, *Security Interests in Personal Property* § 35.5 (1965); *In re Eshleman,* 10 U.C.C. Rep. Ser. 750 (E.D. Pa. 1972); *John Miller Supply Co., Inc.* v. *Western State Bank,* supra; *National Bank of Eastern Arkansas* v. *Blankenship,* 177 F. Supp. 667 (E.D. Ark. 1959).

The true intention of the parties is really the sole and controlling factor in determining whether the future advances were covered by the original agreement. If the parties intended to deal on a single loan basis, intending an entirely new transaction each time, then each new agreement would have to be reperfected. *John Miller Supply Co., Inc.* v. *Western State Bank,* supra; *In re Sanelco,* 7 U.C.C. Rep. Ser. 65 (M.D. Fla. 1969); *In re Glawe,* 6 U.C.C. Rep. Ser. 876 (E.D. Wis. 1969); *Coin-O-Matic Service Co.* v. *Rhode Island Hospital Trust Co.,* 3 U.C.C. Rep. Ser. 1112 (R.I. 1966).

After reviewing the facts of this case, the Court is of the opinion that it was not the intention of O.K. Super Markets and Kimbell Foods for the later purchases on open account to be secured by the future advance clauses in the 1966 and 1968 agreements. The parties treated each as a separate and distinct agreement and each was for a specific nonrecurring purpose. The 1966 agreement was entered into to enable O.K. Super Markets to expand to a new location by delaying the payment of a balance owing Kimbell

Foods. This was not related in any way to the later inventory purchases on open account by O.K. Super Markets. Likewise, the 1968 agreements were entered into for the purpose of delaying the payment of a balance owing Kimbell Foods so that O.K. Super Markets could pay off a debt owing Associated Grocers, Inc. The later purchases on open account were simply not of the same class as the primary indebtedness. As shown by the testimony of the president of O.K. Super Markets, the parties intended each transaction to be separate and distinct and each agreement was renegotiated and reperfected. It is the judgment of this Court that the parties did not intend for the "boiler plate" future advance clauses in the three agreements to secure the later purchases on open account.

For this reason, as well as the fact that the lien of the plaintiff was not choate at the time the lien of the United States arose, the Court finds that the claim asserted herein by the United States should prevail over that of Kimbell Foods.

State and City Sales Tax Liens

Against the proceeds held in escrow, the State of Texas and City of Dallas claim certain sums for sales taxes that were due and payable by O.K. Super Markets when the three stores were sold in 1971. Although acknowledging that federal law is applicable to this case, the intervenors contend that there is a federal statute, 15 U.S.C. § 646,[7] which subordinates

[7] 15 U.S.C.A. § 646 provides as follows: "Any interest held by the Administration in property, as security for a loan, shall be subordinate to any lien on such property for taxes due on the property to a State, or political subdivision thereof, in any case

a SBA lien to state and city taxes that are accorded priority under state law.

It is true that under the law of Texas, Article 1.07 of Title 122A, *Tex. Rev. Civ. Stat. Ann.*, the State and City have a preferred lien for taxes, penalties and interest that is first and prior to all others. Under state law these liens attach to all the property of the debtor and they become effective when the taxes are due and owing. *State* v. *Smith*, 434 S.W. 2d 342 (Tex. 1968); *Pecos County State Bank* v. *State*, 468 S.W. 2d 867 (Tex. Civ. App.—Austin, 1971, writ ref'd n.r.e.).

If the intervenors are entitled to pursue the proceeds into the escrow account, and if §646 is applicable to their claim, then it is clear that they would stand first in line. However, if §646 is inapplicable, then under the choate lien test the intervenors would only be entitled to those taxes that became due and payable by February of 1969, when the SBA lien became choate. This is assuming of course that the intervenors are entitled to pursue the proceeds of the private sale of the three stores.

The problem with the intervenors' argument as it pertains to § 646 is that the decisions construing this section have been uniform in their holdings that general taxes, such as sales taxes, are not taxes due on specific property and thus do not come within the ambit of §646. See *United States* v. *City of Albuquerque, New Mexico*, supra; *Director of Revenue* v. *United States*, supra; *United States* v. *Clover Spinning Mills Company*, 373 F. 2d 274 (4th Cir. 1966); Annot., 17 A.L.R. Fed. 874 (1973). Even

where such lien would, under applicable State law, be superior to such interest if such interest were held by any party other than the United States."

where the liens asserted are for ad valorem taxes and thus entitled to priority, the Courts have disallowed claims for penalties and interest under §646. *United States* v. *Consumers Scrap Iron Corporation,* 384 F. 2d 62 (6th Cir. 1967); *United States* v. *Christensen,* 218 F. Supp. 722 (D. Mont. 1963).

Aside from the questions under § 646, the government makes a strong attack on the intervenors' right to assert their liens against the proceeds held in escrow. After reviewing the applicable authorities, the Court believes that the position taken by the United States is correct and finds that the intervenors are not entitled to assert their liens against the proceeds held in escrow.

As noted previously, these proceeds are from the sale of three stores, which were sold pursuant to a written agreement entered into between Republic Bank and O.K. Super Markets and approved by the United States and Kimbell Foods. It was a contract with consideration flowing both ways and it was entered into to obtain funds for the settlement of the conflicting claims of the parties to the agreement.

Generally it may be said that a lien can follow the proceeds of the sale of property where the lien has been "destroyed" by either wrongful conversion or sale to an innocent purchaser for value. However, if the lien is not destroyed then the lienor has no right to the proceeds and the lien must follow the property. 51 Am. Jur. 2d Liens § 60 (1970); 33 C.J.S. Executions § 248 (1942).

Here, the liens held by the State and City were not extinguished or destroyed by the bulk sale of the collateral. Article 20.09 of Title 122A, *Tex. Rev. Civ.*

Stat. Ann., provides that the purchaser of a business or stock of goods must withhold a sufficient amount of the purchase price to cover the sales taxes owed by the vendor. If he fails to withhold such an amount, he becomes personally liable. It is also clear that the lien on property purchased from O.K. Super Markets is still valid and enforceable against the property in the hands of the purchasers. See *Pecos County State Bank* v. *State,* supra.

The State entered into certain releases with the purchasers of the stores. While these agreements released the purchasers from *personal liability,* they expressly provided that they did not "* * * release any claim or lien on any property bought from O.K. Super Markets, Inc. * * *." These purchasers cannot be classified as bona fide purchasers who are protected from the tax liens, because they purchased the property with full knowledge of the existence of such liens. For these reasons, the Court concludes that the intervenors are not entitled to a portion of the proceeds being held in escrow by Republic Bank for sales taxes, penalties and interest.

AD VALOREM TAXES OF THE CITY OF DALLAS

The intervenor City of Dallas is asserting a claim for delinquent ad valorem personal property taxes that were owing to the City and the Dallas Independent School District for the years 1969, 1970, 1971 and 1972, when the stores were sold by O.K. Super Markets. The city seeks a total of $2,530.10 which represents $1,933.57 in delinquent taxes and $596.53 in penalties and interest.

Of course, if the intervenor is entitled to pursue the proceeds, then 15 U.S.C.A. § 646, would subordinate the claim of the United States to this ad valorem tax claim because these are taxes due on specific property. See Annot. 17 A.L.R. Fed. 874 (1973). In this regard, Chapter 19, Section 14 of the Charter of the City of Dallas gives priority to ad valorem taxes over all other claims.[8] However, the Court entertains some doubt as to whether the Dallas Independent School District would have a specific statutory lien on personal property. See *City of San Marcos* v. *Zimmerman,* 361 S.W. 2d 929, 935 (Tex. Civ. App.—Austin, 1962, writ ref'd n.r.e.). The Court also would question whether the City of Dallas is entitled to assert a claim on behalf of a separate legal entity that is not a party to this suit.

However, it is not necessary to make these determinations because the Court feels that the City of Dallas is not entitled to pursue the proceeds in escrow. Just like the liens for sales taxes, the City's lien for ad valorem taxes was not destroyed by the bulk sale of the collateral, and the City is entitled to pursue the subject property into the hands of the purchasers. See *Pecos County State Bank* v. *State,* supra. Pursuant to Article 1060a, *Tex. Rev. Civ. Stat. Ann.,* a city or school district is given the right to employ any of the previously discussed methods for the collection of taxes that are available to the State or a county. See 54 Tex. Jur. 2d Taxation § 142 n. 1. Therefore, the Court concludes that the City of Dallas is not entitled to assert the claim for ad valorem taxes against the proceeds in escrow.

[8] This Charter provision provides as follows: "A lien is hereby created on all property, personal and real in favor of the City of Dallas, for all taxes, ad valorem, occupation or otherwise. Said lien shall exist from January 1st in each year until the taxes are paid. Such lien shall be prior to all other claims, and no gift, sale, assignment or transfer of any kind, or judicial writ of any kind, can ever defeat such lien, but the director of revenue and taxation may pursue such property, and whenever found may seize and sell enough thereof to satisfy such taxes."

CONCLUSION

In summary, the Court finds that the United States is entitled to the entire sum being held in escrow by the Republic National Bank of Dallas. The United States prevails over Kimbell Foods for two reasons. In the first place, the lien asserted by the plaintiff was not sufficiently specific to satisfy the federal choate lien test until after the lien of the United States became choate. Secondly, the future advances of inventory on open account were not secured by the 1966 and 1968 security agreements. As to the tax claims of the intervenors, the Court concludes that pursuant to state statute these intervenors have full recourse against the bulk purchasers of the stores and the property purchased. Therefore, these tax liens were not destroyed by the sale of the property and the intervenors have no right to pursue the proceeds in escrow.

Judgment will be entered in accordance with the findings made herein.

Signed and entered this 5th day of September, 1975.

WILLIAM M. STEGER,
United States District Judge.

In the United States District Court for the Northern District of Texas, Dallas Division

(Civil Action No. 3-74-56-D)

Filed October 1, 1975

KIMBELL FOODS, INC., A CORPORATION, F/K/A/ KIMBELL MILLING COMPANY, D/B/A/ KIMBELL GROCERY COMPANY, PLAINTIFF,

v.

REPUBLIC NATIONAL BANK OF DALLAS AND UNITED STATES OF AMERICA, DEFENDANTS, AND STATE OF TEXAS AND CITY OF DALLAS, INTERVENORS.

JUDGMENT

The above entitled cause came on regularly for trial before the Court without a jury, after due notice to all parties, and, after hearing the evidence and argument of counsel and considering the pleadings and briefs, the Court rendered its decision on the 5th day of September, 1975, by its Memorandum Opinion, which was filed on the 8th day of September, 1975, and in which appeared the findings of fact and conclusions of law of the Court.

It is, therefore, ORDERED, ADJUDGED, and DECREED that the Plaintiff, Kimbell Foods, Inc., f/k/a/ Kimbell Milling Company, d/b/a/ Kimbell Grocery Company, is not entitled to any portion of the sum held in escrow by the Republic National Bank of Dallas pursuant to the agreement of February 3, 1971, between the said Bank and O.K. Super Markets, Inc., and approved as to form and substance by

the Small Business Administration of the United States of America and the said Kimbell Foods, and all relief sought by the said Plaintiff against Republic National Bank of Dallas and the United States of America is denied.

It is further ORDERED, ADJUDGED, and DECREED that the Intervenors, the State of Texas and the City of Dallas, are not entitled to any portion of the sum held in escrow by the Republic National Bank of Dallas pursuant to the aforesaid agreement of February 3, 1971, and all relief sought by the said Intervenors against Republic National Bank of Dallas and the United States of America is denied.

It is further ORDERED, ADJUDGED, and DECREED that all sums held in escrow by the Republic National Bank of Dallas pursuant to the aforesaid agreement of February 3, 1971, the said sum being $100,836.03 as of September 15, 1975, be recovered by and paid over to the Defendant, the United States of America, pursuant to the aforesaid Memorandum Opinon of this Court.

It is further ORDERED, ADJUDGED, and DECREED that the Defendants, the United States of America and Republic National Bank of Dallas, have and recover the costs of this proceeding from the Plaintiff, Kimbell Foods, Inc.

Entered this 29th day of September, 1975.

WILLIAM M. STEGER,
United States District Judge.

APPENDIX D

UNITED STATES COURT OF APPEALS,
FIFTH CIRCUIT,
OFFICE OF THE CLERK,
New Orleans, La., October 25, 1977.

To all parties listed below:

No. 75-4105—*Kimbell Foods, Inc., Etc.* v. *Republic Nat'l. Bank of Dallas, et al, The State of Texas, et al.*

DEAR COUNSEL: This is to advise that an order has this day been entered denying the petition( ) for rehearing,** and no member of the panel nor Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc (Rule 35, Federal Rules of Appellate Procedure; Local Fifth Circuit Rule 12) the petition( ) for rehearing en banc has also been denied.

See Rule 41, Federal Rules of Appellate Procedure for issuance and stay of the mandate.

Very truly yours,
EDWARD W. WADSWORTH,
Clerk.
BRENDA M. HAUCK,
Deputy Clerk.

**On behalf of appellee, U.S.A.

U.S. GOVERNMENT PRINTING OFFICE: 1978

APPENDIX

IN THE
Supreme Court of the United States
OCTOBER TERM, 1978

No. 77-1359

UNITED STATES OF AMERICA,
Petitioner,

—*v.*—

KIMBELL FOODS, INC., ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE FIFTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI FILED MARCH 24, 1978
CERTIORARI GRANTED MAY 15, 1978

IN THE

Supreme Court of the United States

OCTOBER TERM, 1978

No. 77-1359

UNITED STATES OF AMERICA,

Petitioner,

—*v.*—

KIMBELL FOODS, INC., ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

INDEX

CIVIL DOCKET

UNITED STATES DISTRICT COURT

CA 3 74-56-D

KIMBELL FOODS, INC., a corporation f/k/a KIMBELL MILLING COMPANY d/b/a KIMBELL GROCERY COMPANY,
PLAINTIFFS

THE STATE OF TEXAS and THE CITY OF DALLAS, TEXAS,
INTERVENING PLAINTIFFS

vs.

REPUBLIC NATIONAL BANK OF DALLAS and
UNITED STATES OF AMERICA, DEFENDANTS

RELEVANT DOCKET ENTRIES

DATE	PROCEEDINGS
1974	
Jan. 22	Received and Filed the following from the Fort Worth Division, U.S. District Court, Northern District of Texas:
1972	
Nov. 15	Filed ORDER on Court's own motion to transfer to docket of Hon. Leo Brewster, Ft. Worth Div., ND/Texas Cys. mld to counsel Orig. & duplicate file w/certified copy of Order of Transfer mld to Ft. Worth Div. along with certified copy of dkt entries
Nov. 17	Received FILE
	5/4/72—Filed ORIGINAL COMPLAINT and issued SUMMONS (5)

DATE	PROCEEDINGS
5/9/72	Filed MARSHALS RETURN ON SUMMONS (2) executed 5/5/72 by serving Republic Natl Bank by delivering to Robert P. Martin; the United States by serving Eldon Mahon to Kenneth Mighell; Atty Gen. by certified mail; Small Business Adm. by certified mail.
5/24/72	Filed ORIGINAL ANSWER OF DEFENDANT; REPUBLIC NATIONAL BANK OF DALLAS
7/5/72	Filed ORIGINAL ANSWER of DEFENDANT, UNITED STATES of AMERICA
1973	
Mar. 30	Filed MOTION of the State of Texas For Leave to Intervene
Mar. 30	Filed BRIEF in Support of the State's Motion to Intervene
Apr. 9	Filed Defendant Republic National Bank of Dallas REPLY to the Motion for Leave to Intervene
Apr. 16	Filed ORDER (allowing intervention of The State of Texas and the City of Dallas)
Apr. 16	FILED INTERVENORS COMPLAINT (State of Texas, and City of Dallas, Texas)
Apr. 16	Attorneys of Record notified.
Jun. 19	Filed ANSWER of U.S.A. to Intervenor's Complaint.
Jun. 21	Filed Defendant Republic National Bank of Dallas's ANSWER to Intervenors' Complaint
Jun. 27	Filed Defendant United States Of America's INTERROGATORIES pursuant to Rule 33 to the State of Texas
Jun 27	Filed Defendant United States of America's INTERROGATORIES pursuant to Rule 33 to the City of Dallas
Jul. 13	Filed PRE-TRIAL ORDER TRIAL SET FOR (9:30 AM, September 17, 1973 Probable length of trial in this case is 1/2 day

DATE	PROCEEDINGS
Jul. 13	Filed Supplemental PRE-TRIAL ORDER
Sep. 12	Filed Plaintiff's ANSWER to Intervenors' Complaint
Nov. 8	Filed INTERVENTION of the City of Dallas
1974	
Jan. 21	Filed ORDER THAT ON Consideration of the Court's own motion to transfer the above styled and numbered cause for the reason
Jan. 21	that this Court is disqualified. It is Ordered that the above-styled cause be and is hereby transferred to the Dallas Division, Northern District of Texas. Attorneys Notified
Jan. 21	Original file mailed to Dallas Division
Feb. 11	Vernon O. Teofan—Attorney for Kimbell—Lewis A. Jones—Assistant Attorney General of Texas—Ted MacMaster, City of Dallas, Roger Allen—U.S. Attorney's Office—Frank Betancourt—Republic National Bank of Dallas Hearing on status of case—case to be set in March 1974.
May 21	Filed letter of appearance of Catherine B. Jacob & Gordon C. Cass as attorneys for the State of Texas.
May 28	Filed ANSWER OF INTERVENOR, THE STATE OF TEXAS, TO INTERROGATORIES OF THE DEFENDANT, THE U.S.A.
June 25	Filed PLAINTIFF'S ANSWED TO INTERVENTION OF CITY OF DALLAS
July 8	Filed STIPULATION.
July 8	Filed MEMORANDUM BRIEF IN SUPPORT OF PRIORITY OF TAX LIEN OF CITY OF DALLAS FOR AD VALOREM TAXES by Intervenor City of Dallas.

DATE	PROCEEDINGS

July 8 Filed STIPULATION OF ATTORNEY'S FEES.

July 15 Filed ANSWER OF REPUBLIC NATIONAL BANK OF DALLAS TO INTERVENTION OF CITY OF DALLAS.

Jul. 15 CASE TO TRIAL, 2:00 p.m., before Judge William M. Steger. A. L. Vickers for plaintiff; Chas. D. Cabiness for Small Business Administration; Ted P. McMaster for City of Dallas; Catherine Jacob for State of Texas; Frank Betancount for defendant Republic National Bank. At close of evidence, Court instructed counsel for Plaintiff to submit written Brief by August 5, 1974. All other parties to file Answers to Plaintiff's Brief by August 26, 1974. Case will be taken under advisement. (Mr. Vickers will bring in all Exhibits, both Plaintiff and Defendant, to be submitted to Judge Steger, when he files his Brief on August 5, 1974.) Adjourned 3:15 p.m.

July 29 Filed TRIAL BRIEF OF THE STATE OF TEXAS, INTERVENOR.

Aug. 5 Filed PLAINTIFF'S BRIEF IN SUPPORT OF MOTION FOR JUDGMENT.

Aug. 26 Filed DEFENDANT'S MOTION FOR EXTENSION OF TIME IN WHICH TO MOVE, ????? OR OTHERWISE PLEAD.

Sept. 3 Filed ORDER GRANTING EXTENSION OF TIME.
Copies to attorneys of record.

Sept. 3—Filed POST-TRIAL BRIEF OF DEFENDANT UNITED STATES OF AMERICA.

Sep. 6 Filed PLAINTIFF'S REPLY BRIEF

1975

Sept. 8 Filed MEMORANDUM OPINION.
Certified copies to counsel.

DATE	PROCEEDINGS

Oct. 1 Filed JUDGMENT after trial before the Court without a jury. It is ORDERED that Plaintiff is not entitled to any portion of the sum held in escrow by Republic National Bank of Dallas pursuant to the agreement of Feb. 3, 1971, between said Bank and O. K. Super Markets, Inc., and approved by the Small Business Administration of the U.S.A. and said Kimbell Foods; all relief sought by Plaintiff against Republic National Bank of Dallas and the U.S.A. is denied. It is further ORDERED that the Intervenors, the State of Texas and the City of Dallas, are not entitled to any portion of the sum held in escrow and all relief sought by said Intervenors against Republic National Bank of Dallas and the U.S.A. is denied. It is ORDERED that the sum of $100,836.03 held in escrow by the Republic National Bank of Dallas as of Sept. 15, 1975, be recovered by and paid over to the Defendant, the U.S.A. It is ORDERED that the Defendants, the U.S.A. and Republic National Bank of Dallas, have and recover the costs of this proceeding from the Plaintiff, Kimbell Foods, Inc.
Copies mailed to counsel.

Oct. 7 Filed BILL OF COSTS in the amount of $20.00.

Oct. 28 Filed Plaintiff's NOTICE OF APPEAL from the final judgment entered October 1, 1975.

Oct. 28 Filed Plaintiff's BOND FOR COST ON APPEAL.

Oct. 29 Mailed copy of NOTICE OF APPEAL with copy of docket sheet to 5th Circuit.

Oct. 29 Mailed copies of NOTICE OF APPEAL to all counsel of record.

Dec. 8 Filed ORDER that the time within which to file the record and docket the above-entitled cause in the U.S. Court of Appeals for the 5th Circuit be and the same is hereby extended to and including 1-27-76.
Copies mailed to all counsel of record on 12-09-75.

DATE	PROCEEDINGS

Dec. 9 Mailed certified copy of ORDER extending the time to docket the record on appeal. (Air-Mail to Mr. Wadsworth) 5th Circuit Court of Appeals. (Extended to Jan. 27, 1976.)

1976

Jan. 26 Mailed original case papers to Court of Appeals-Transcript to follow with listed exhibits.

DOCKET
UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 75-4105

Date Docketed: 11-19-75

Date Notice of Appeal Filed: 10-28-75

[Caption Omitted]

3-8-76 Brief for Appellant (M)

3-31-76 Brief for Appellee (USA) (M)

4-7-76 Reply Brief for Appellant (M)

3-18-76 Appellee, Rep. Nat'l. Bank, adoptg. brief of U.S.A.

4-18-77 Case argued, HT—TGG—MARKEY

8-12-77 Opinion rendered—reversed, TGG

8-24-77 Rehearing—Mot. for Ext.—Ext. to 9-26-77 (Appellee)

9-26-77 Petition for Rehearing (M) (J)—Appellee (U.S.A.)

10-25-77 Order Denying Rehearing (en banc)

Nov. 2, 1977 Jdgt. as Mdt. Issd. to Clerk

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

Civil Action No. CA-3-5835-C

KIMBELL FOODS, INC., A Corporation,
f/k/a KIMBELL MILLING COMPANY,
d/b/a KIMBELL GROCERY COMPANY, PLAINTIFF

vs.

REPUBLIC NATIONAL BANK OF DALLAS AND
UNITED STATES OF AMERICA, DEFENDANTS

ORIGINAL COMPLAINT

TO THE HONORABLE JUDGE OF SAID COURT:

Now comes KIMBELL FOODS, INC., A Corporation, f/k/a KIMBELL MILLING COMPANY, d/b/a KIMBELL GROCERY COMPANY, Plaintiff, and files this, its Original Complaint, complaining of REPUBLIC NATIONAL BANK OF DALLAS and UNITED STATES OF AMERICA, Defendants, and for cause of action, Plaintiff would show the Court the following:

I.

This Court has jurisdiction of this cause of action by virtue of the provisions of Title 28, Section 2410 of the United States Code, this suit being brought by Plaintiff to quiet title to and to foreclose its liens upon personal property in which the UNITED STATES has or claims a security interest.

II.

Plaintiff, KIMBELL FOODS, INC., is a corporation duly incorporated and existing under and by virtue of the laws of the State of Texas, with its principal office and place of business in Forth Worth, Tarrant County, Texas and was formerly known as KIMBELL MILLING COMPANY and did business as KIMBELL GROCERY COMPANY.

Defendant, REPUBLIC NATIONAL BANK OF DALLAS, is a national banking corporation organized under the laws of the United States of America, with its principal office and place of business in Dallas, Dallas County, Texas where process may be served upon its president or any vice president.

Defendant, UNITED STATES OF AMERICA, is herein sued on behalf of its agency, Small Business Administration. Service of process may be made by serving a copy of this complaint upon the United States Attorney for the Northern District of Texas, or upon any Assistant United States Attorney in writing filed with the Clerk of this Court and by sending copies of the process and complaint herein by certified mail to the Attorney General of the United States of America at Washington, District of Columbia.

III.

On or about August 4, 1966, O. K. Super Markets, Inc., for good and valuable consideration, made, executed and delivered to Plaintiff, its Security Agreement and Financing Statement granting Plaintiff a security interest in therein listed equipment and in fixtures and all goods, wares and merchandise and any and all additions or accessions thereto to secure payment of the therein described promissory note and all extensions and renewals thereof and all other indebtedness at any time thereafter owing by O. K. Super Markets, Inc. to Plaintiff as well as the discharge of all obligations imposed upon O. K. Super Markets, Inc. thereunder. Attached hereto marked Exhibit "A" and made a part hereof is an exact copy of said Security Agreement and Financing Statement which was filed with the Secretary of State of Texas on September 2, 1966.

IV.

On or about April 17, 1968, said O. K. Super Markets, Inc. for good and valuable consideration, made, executed and delivered to the Plaintiff, its Security Agreement

and Financing Statement granting to Plaintiff a security interest in therein described equipment and in all other furniture, fixtures and equipment, all goods, wares, merchandise and stock in trade and any and all additions and accessions thereto to secure the payment of the therein described promissory note and all extensions and renewals thereof and all other indebtedness at any time thereafter owing by O. K. Super Markets, Inc. to Plaintiff as well as the discharge of all obligations imposed upon O. K. Super Markets, Inc. thereunder. Attached hereto marked Exhibit "B" and made a part hereof is an exact copy of said Security Agreement and Financing Statement which was filed with the Secretary of State of Texas on April 22, 1968.

V.

On or about November 7, 1968, said O. K. Super Markets, Inc. for good and valuable consideration, made, executed and delivered to the Plaintiff, its Security Agreement and Financing Statement granting to Plaintiff a security interest in therein described equipment and in all goods, wares, merchandise and accounts and any and all additions and accessions thereto to secure the payment of the therein described promissory note and all extensions and renewals thereof and all other indebtedness at any time thereafter owing by O. K. Super Markets, Inc. to Plaintiff as well as the discharge of all obligations imposed upon O. K. Super Markets, Inc. thereunder. Attached hereto marked Exhibit "C" and made a part hereof is an exact copy of said Security Agreement and Financing Statement which was filed with the Secretary of State of Texas on November 21, 1968.

VI.

Said hereinabove referred to three (3) Security Agreements and Financing Statements were cumulative of each other and the Security Agreements marked Exhibits "B" and "C" were in addition and in extension of the Security Agreement and Financing Statement, a copy of which is attached hereto and marked Exhibit "A", and under

the laws of the State of Texas, Plaintiff's security interest in the collateral described in said Security Agreements and Financing Statements became duly perfected as of September 2, 1966.

VII.

On or about August 7, 1968 said O. K. Super Markets, Inc. executed and delivered to Defendant, REPUBLIC NATIONAL BANK OF DALLAS, its Financing Statement covering all the debtor's machinery, fixtures, equipment and inventory then existing or thereafter acquired, all replacements and substitutes therefor, all accessions, attachments and additions thereto, and all tools, parts and equipment then or thereafter added to or used in connection with such machinery and equipment, and all similar property thereafter acquired by debtor to secure the payment of funds loaned by REPUBLIC NATIONAL BANK OF DALLAS to O. K. Super Markets, Inc., 90% of which loan was guaranteed by the Small Business Administration of the UNITED STATES OF AMERICA. Attached hereto marked Exhibit "D" is a copy of said Financing Statement which was filed with the Secretary of State of Texas on August 7, 1968. The collateral described in said Financing Statement is also described and included in the Security Agreements and Financing Statements of Plaintiff and said Financing Statement of REPUBLIC NATIONAL BANK OF DALLAS is in partial conflict with the Security Agreements and Financing Statements of Plaintiff.

VIII.

On January 15, 1971, Plaintiff filed suit in the 96th Judicial District Court of Tarrant County, Texas, Cause No. 96-5548-70 against said O. K. Super Markets, Inc., and others to recover, among other things, judgment against said O. K. Super Markets, Inc. for its indebtedness to Plaintiff in the amount of $18,258.57 principal, plus interest, reasonable contractual and statutory attorneys' fees, costs of suit and for foreclosure of its security interest in the collateral described in the Security Agree-

ments, copies of which are attached hereto marked Exhibits "A", "B" and "C".

IX.

On or about February 3, 1971, an agreement was entered into by and between said O. K. Super Markets, Inc. and Defendant REPUBLIC NATIONAL BANK OF DALLAS and approved as to form and substance by the Defendant Small Business Administration of the UNITED STATES OF AMERICA and Plaintiff, whereunder the collateral covered by the Security Agreements and Financing Statements of Plaintiff, copies of which are attached hereto marked Exhibits "A", "B", and "C", was to be sold and liquidated with the proceeds thereof to be held in escrow by Defendant REPUBLIC NATIONAL BANK OF DALLAS pending a resolution of the above-referred to cause of action No. 96-5548-70 filed in the 96th Judicial District Court of Tarrant County, Texas and to be paid over to the party or parties in the manner and amounts as finally determined to be legal and rightful. Attached hereto marked Exhibit "E" is a true and correct unsigned copy of said agreement.

X.

Thereafter, on or about February 8, 1971 the collateral located at O. K. Super Markets, Inc., store No. 14, 3805 Kiest Boulevard, Dallas, Dallas County, Texas, was sold to Pat H. Hood for the total sum of $30,000.00, $18,000.00 thereof being attributable to the inventory of stock in trade and $12,000.00 thereof to the fixtures, equipment and other property. Attached hereto marked Exhibit "F" is a true and correct copy of the Contract of Sale under which said collateral was sold to Pat H. Hood.

XI.

On or about February 8, 1971 the collateral located at O. K. Super Markets, Inc., store No. 5, 3026 Grand Avenue, Dallas, Dallas County, Texas, was sold to Grand City Groceries, Inc. for a total price of $30,000.00, $18,000.00 thereof being attributable to the inventory

of stock in trade and $12,000.00 thereof to the fixtures, equipment and other porperty. Attached hereto marked Exhibit "G" is a true and correct copy of the Contract of Sale under which said collateral was sold to Grand City Groceries, Inc.

XII.

On or about February 8, 1971 the collateral located at O. K. Super Markets, Inc., store No. 3, 1903 South Ervay Street, Dallas, Dallas County, Texas, was sold to Charles W. Logan for the total price of $35,000.00, $21,000.00 thereof being attributable to the inventory of stock in trade and $14,000.00 thereof to the fixtures, equipment and other property. Attached hereto marked Exhibit "H" is a true and correct copy of the Contract of Sale under which said collateral was sold to Charles W. Logan.

XIII.

Thereafter, by amended petition, REPUBLIC NATIONAL BANK OF DALLAS was made a party Defendant in said Cause No. 96-5548-70 in the 96th Judicial District Court of Tarrant County, Texas and thereafter said cause as it pertained to said REPUBLIC NATIONAL BANK OF DALLAS was transferred upon the Plea of Privilege of REPUBLIC NATIONAL BANK OF DALLAS to the 134th Judicial District Court of Dallas County, Texas where it remains pending.

XIV.

On January 31, 1972, judgment was entered in said Cause No. 96-5548-70 in favor of Plaintiff and against O. K. Super Markets, Inc. in the sum of $18,258.57 principal, $1,186.80 interest and reasonable statutory attorneys' fees in the sum of $5,000.00 and granting foreclosure of said security interests as the same existed on August 4, 1966, April 17, 1968 and November 7, 1968 in and to all property as reflected in said three (3) Security Agreements, copies of which are attached hereto marked Exhibits "A", "B" and "C". Attached hereto

marked Exhibit "I" and made a part hereof is a true and correct copy of said judgment.

XV.

REPUBLIC NATIONAL BANK OF DALLAS holds in escrow under said agreement of February 3, 1971, sufficient cash sums to pay said Plaintiff's judgment in full and although due demand has been made upon said Defendant, REPUBLIC NATIONAL BANK OF DALLAS, said bank has wholly failed and refused to pay said sums to Plaintiff.

XVI.

Plaintiff is informed and believes that the Small Business Administration of the UNITED STATES OF AMERICA has paid to REPUBLIC NATIONAL BANK OF DALLAS 90% of O. K. Super Markets, Inc.'s indebtedness to the REPUBLIC NATIONAL BANK OF DALLAS which was in the amount of $252,331.93 on February 3, 1971 and has accordingly been assigned a proportionate interest in the security interest held by REPUBLIC NATIONAL BANK OF DALLAS in said property of O. K. Super Markets, Inc. described in the Financing Statement, a copy of which is attached hereto as Exhibit "D", and that the Small Administration of the UNITED STATES OF AMERICA is now asserting said security interest in said collateral.

XVII.

That Plaintiff's security interest in the property of O. K. Super Markets, Inc. sold under said agreement of February 3, 1971 was duly perfected as of September 2, 1966 and is prior to time, prior in right and superior to the security interest therein asserted by Defendant REPUBLIC NATIONAL BANK OF DALLAS and its assignee, Defendant Small Business Administration of the UNITED STATES OF AMERICA and that Plaintiff is entitled to the proceeds realized from the sale thereof being held by Defendant REPUBLIC NATIONAL BANK OF DALLAS to the extent of the indebtedness due and

owing to it by O. K. Super Markets, Inc., as evidenced by said judgment of January 31, 1972.

WHEREFORE, PREMISES CONSIDERED, Plaintiff prays the Court that service of process be had on said Defendants and that on final hearing hereof, Plaintiff recover judgment declaring its security interest in the property of O. K. Super Markets, Inc. sold pursuant to said agreement of February 3, 1971 prior and superior to the security interest asserted by Defendants REPUBLIC NATIONAL BANK OF DALLAS and UNITED STATES OF AMERICA and for judgment against REPUBLIC NATIONAL BANK OF DALLAS in the sum of $24,445.37 together with interest thereon at the rate of 6% per annum from February 4, 1972, together with all costs of Court incurred in said Cause No. 96-5548-70 and incurred herein, and for such other and further relief, as may be just.

UNGERMAN, HILL, UNGERMAN, ANGRIST, DOLGINOFF & TEOFAN
Attorneys for KIMBELL FOODS, INC., A Corporation, f/k/a KIMBELL MILLING COMPANY, d/b/a KIMBELL GROCERY COMPANY, Plaintiff

By: /s/ Vernon O. Teofan
VERNON O. TEOFAN
820 United Fidelity Building
Dallas, Texas 75202—747-3536

EXHIBIT A

FILING OFFICE COPY - UCC-21

4. Maturity Date (if any)

1. Debtor
O K SUPER MARKETS, INC.
1903 S. Ervay
Dallas, Tex.

2. Secured Party
KIMBELL MILLING CO. DBA
KIMBELL GROCERY COMPANY
P. O. Box 1540
Ft. Worth, Tex.

3. For Filing Officer
JOHN L. HILL
SECRETARY OF STATE
FILED 8:30 AM

Assignee

SEP 26 032709

X ☐ Nonstandard Form F. S.

☒ See Oversize File No. O-4128

☐ Cross Reference. See:

(2) FILING OFFICER COPY - ACKNOWLEDGEMENT

STANDARD FORM UCC-21 — Approved by the Secretary of State of Texas

SECURITY AGREEMENT AND FINANCING STATEMENT

August 4, 1966
(Date)

O. K. Super Markets, Inc., 1903 South Ervay, Dallas, Texas
(Name) (No. and Street) (City) (State)

hereinafter called "Debtor", whether one or more), for a valuable consideration hereby acknowledged, hereby grant(s) to

Kimbell Milling Company d/b/a Kimbell Grocery Company, 1929 South Main, Ft. Worth, Texas
(Name) (No. and Street) (City) (State)

(hereinafter called "Secured Party"), a security interest in the following property and any and all additions and accessions (hereinafter called the "Collateral"): List of collateral attached hereto and made a part hereof:

This security agreement and financing statement is given to secure an advance of goods, wares and merchandise and does not include a pre-existing debt.

to secure payment of a Promissory Note dated August 4, 1966 in the sum of $ 20,000.00, and all extensions and renewals thereof; said security interest also being given to secure the payment of all other indebtedness at any time hereafter owing by Debtor to Secured Party as well as the discharge of all obligations imposed upon Debtor hereunder. If this contract after default is placed in the hands of an attorney, the Debtor will pay the Secured Party a reasonable attorney's fee not exceeding 10% of the unpaid principal and interest, such payment to be secured by the Security Interest herein created.

Debtor further agrees and warrants:

(a) The Collateral is bought or used primarily for: ( ) Personal, family or household purposes; ( ) Farming operations; (X) For use in the operation of a business or profession. If checked here (X), the collateral is being acquired, in whole or in part, with the proceeds of the above mentioned advance; and the Secured Party is authorized to make such advance direct to the seller.

(b) The Collateral will be kept at 912 Corinth Street, Dallas, Texas
(Street Address) (City) (State)
or if the last preceding space is left blank, it will be kept at the address shown at the beginning of this agreement.

(c) If the collateral is bought or used primarily for business use, the Debtor maintains a place of business at the address shown at the beginning of this Agreement; and all other places of business (if any) of Debtor are located as follows:
1146 Pearcy Rd. 3026 Grand Ave. 2900 So. Lamar 4630 Hatcher 4820 E. Grand (Dallas, Tex
5109 Bexar St. 4121 Colonial 4123 Oakland 3227 Pennsylvania 3016 Weatherford Ave.
(If no other places of business insert "None")

(d) If the Collateral is to be attached to real estate, a description of the real estate is as follows:
Not Applicable
(If not attached to real estate, insert "NOT APPLICABLE")
and the name of the record owner is Not Applicable

If the Collateral is attached to real estate prior to the perfection of the security interest granted hereby, Debtor will on demand of Secured Party furnish the latter with a disclaimer or disclaimers, signed by all persons having an interest in the real estate, of any interest in the Collateral which is prior to Secured Party's interest.

THIS AGREEMENT IS SUBJECT TO THE ADDITIONAL PROVISIONS SET FORTH ON THE REVERSE SIDE HEREOF, THE SAME BEING INCORPORATED HEREIN BY REFERENCE.

IN WITNESS WHEREOF, the parties hereto have executed this agreement this 30th day of August 1966

Kimbell Milling Company d/b/a
Kimbell Grocery Company
(Secured Party)

By J. L. McCracken
Duly Authorized Agent

O. K. Super Markets, Inc.

By: J. F. Slatter
Debtor

President

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FURTHER AGREEMENTS AND WARRANTIES ON THE PART OF THE DEBTOR

Debtor warrants that As to the Collateral will be good and free of any liens or outstanding interests except the security interest created by this remote agreement.

Without the prior written consent of the Secured Party, when Collateral is fixtures, and, or, equipment Debtor will not sell, exchange, lease or otherwise dispose of the Collateral, or of Debtor's interest therein, and will permit no other lien or security interest to attach to the collateral.

Debor will maintain the collateral in good condition and repair, but without permitting any repairman's lien to attach thereto. Debtor will pay all taxes and assessments imposed upon the Collateral.

Debtor will carry insurance upon the collateral in such amounts, against such hazards, with such insurers and under such forms of policies as may be acceptable to, or requested by, the Secured Party; the insurance policies in every instance to carry mortgage clause in favor of the Secured Party upon such forms as may be approved by it.

When Collateral is fixtures, and, or, equipment Debtor will not permit the Collateral to be removed from its present location as specified herein, except for temporary periods in the normal and customary use hereof, without the prior written consent of the Secured Party. Collateral consisting of goods, wares and merchandise may be sold in the ordinary course of business, but proceeds claimed by Secured Party. Secured Party may inspect the collateral at any time.

Debtor will pay all costs of filing any financing, continuation or termination statements with respect to the security interest created by this agreement; and the Secured Party is hereby appointed Debtor's attorney in fact to do all acts and things which Secured Party may deem necessary to perfect and continue perfected the security interest created by this agreement and to protect the Collateral. No waiver by Secured Party of any default shall operate as a waiver of any other default or of the same default on a future occasion.

All sums at any time expended by the Secured Party for the protection or preservation of the collateral, or of Secured Party's interest therein shall be repayable by Debtor to Secured Party with interest at the rate of 8% per annum; and such repayment shall be secured by the security interest created herein.

If total or partial default is made in the payment at maturity of any sum (principal or interest) at any time secured hereby; or if default is made in the performance of any obligation imposed upon Debtor hereunder; or if any of the representations or warranties of Debtor made in connection with this transaction shall prove to be false; or if any proceeding is instituted by or against the Debtor under the provisions of the Bankruptcy Act or any state insolvency law or in the event of death of Debtor, or if the Secured Party shall at any time deem its rights hereunder insecure — then, in any of such events, the holders of this security interest may at its option declare all indebtedness secured hereby (with all interest accrued thereon) to be immediately due and payable. In such event, the Secured Party may enforce all remedies available to it under the Uniform Commercial Code.

If the Debtor consists of more than one person the liability hereunder is joint and several and all obligations of Debtor shall bind his heirs, executors or administrators or his or its successors or assigns. All rights of the Secured Party will inure to its successors and assigns.

CORPORATION ACKNOWLEDGMENT

THE STATE OF TEXAS,

COUNTY OF Dallas

BEFORE ME, the undersigned, a Notary Public in and for said County and State, on this day personally appeared

Joe Elston, President of O. K. Super Markets, Inc.

known to me to be the person and officer whose name is subscribed to the foregoing instrument and acknowledged to me that the same was the act of the said O. K. Super Markets, Inc. a corporation, and that he executed the same as the act of such corporation for the purposes and consideration therein expressed, and in the capacity therein stated.

GIVEN UNDER MY HAND AND SEAL OF OFFICE this the 31st day of August A.D. 1966.

(L.S.)

Notary Public in and for County, Texas.

a corporation, and was duly authorized in his capacity to execute the foregoing instrument for and in the name and behalf of said corporation, and further stated and acknowledged that he had so signed, executed and delivered said foregoing instrument for the consideration, uses and purposes therein mentioned and set forth.

In testimony whereof I have hereunto set my hand and official seal this 31st day of August, 1966.

My Commission expires July 1967

Notary Public

(Notarial Seal)

File No.____

SECURITY AGREEMENT AND FINANCING STATEMENT

STATE OF_____ ss.
County of_____

I hereby certify that this instrument was filed for record on the____day of_____, A.D., 19____, at_____o'clock____M.

_____ Clerk

By_____ Deputy

_____ Secretary of State

By_____ Deputy

EXHIBIT B

FILING OFFICE COPY — UCC-21

4. Maturity Date (if any):

1. Debtor

O K Supermarkets Inc
1903 S Ervay St
Dallas Texas

2. Secured Party

Kimbell Milling Co
1929 S Main
Ft Worth Texas

3. For Filing Officer

COUNTY CLERK
DALLAS COUNTY

1993 APR 22 PM 11 00

Assignee

☒ Nonstandard Form _____

☐ See Oversize File No. _____

☐ Cross Reference. See:

(2) Acknowledgment

STANDARD FORM—FORM UCC-21—Approved by the Secretary of State of Texas—Form 1568—The Steck Company, Austin, Texas

FILING OFFICE COPY - UCC-21

4. Maturity Date (if any)

Debtor

D. K. Supermarkets, Inc.
1903 So. Ervay
Dallas, Texas

2. Secured Party

Kimbell Milling Company dba
Kimbell Grocery Company
1929 So. Main
Fort Worth, Texas

3. For Filing Officer

SECRETARY OF STATE
FILED 9:00 AM

Assignee

APR 22 63 131992

☒ Nonstandard Form F. S.

☒ See Oversize File No. O-14197

☐ Cross Reference. See:

#1

(2) FILING OFFICER COPY - ACKNOWLEDGEMENT

STANDARD FORM UCC-21 — Approved by the Secretary of State of Texas

SECURITY AGREEMENT AND FINANCING STATEMENT

April 17, 1968
(Date)

O. K. Supermarkets, Inc., 1903 So. Ervay, Dallas, Texas
(Name) (No. and Street) (City) (State)

(hereinafter called "Debtor", whether one or more), for a valuable consideration hereby acknowledged, hereby grant(s) to

Kimbell Milling Company d/b/a Kimbell Grocery Company, 1929 So. Main, Fort Worth, Texas
(Name) (No. and Street) (City) (State)

(hereinafter called "Secured Party"), a security interest in the following property and any and all additions and accessions thereto (hereinafter called the "Collateral"): List of collateral attached hereto and made a part hereof:

to secure payment of a Promissory Note dated April 17, 1968 in the sum of $ 27,000.00, and all extensions and renewals thereof; said security interest also being given to secure the payment of all other indebtedness at any time hereafter owing by Debtor to Secured Party as well as the discharge of all obligations imposed upon Debtor hereunder. If this contract after default is placed in the hands of an attorney, the Debtor will pay the Secured Party a reasonable attorney's fee not exceeding 10% of the unpaid principal and interest, such payment to be secured by the Security Interest herein created.

Debtor further agrees and warrants:

(a) The Collateral is bought or used primarily for: ( ) Personal, family or household purposes; ( ) Farming operations; (X) For use in the operation of a business or profession. If checked here ( ), the collateral is being acquired, in whole or in part, with the proceeds of the above mentioned advance; and the Secured Party is authorized to make such advance direct to the seller.

(b) The Collateral will be kept at List attached and marked exhibit "B"
(Street Address) (City) (State)
or if the last preceding space is left blank, it will be kept at the address shown at the beginning of this agreement.

(c) If the collateral is bought or used primarily for business use, the Debtor maintains a place of business at the address shown at the beginning of this Agreement; and all other places of business (if any) of Debtor are located as follows: List attached and marked exhibit "C"
(If no other places of business insert "None")

(d) If the Collateral is to be attached to real estate, a description of the real estate is as follows: Not applicable
(If not attached to real estate, insert "NOT APPLICABLE")

and the name of the record owner is

If the Collateral is attached to real estate prior to the perfection of the security interest granted hereby, Debtor will on demand of Secured Party furnish the latter with a disclaimer or disclaimers, signed by all persons having an interest in the real estate, of any interest in the Collateral which is prior to Secured Party's interest.

THIS AGREEMENT IS SUBJECT TO THE ADDITIONAL PROVISIONS SET FORTH ON THE REVERSE SIDE HEREOF, THE SAME BEING INCORPORATED HEREIN BY REFERENCE.

IN WITNESS WHEREOF, the parties hereto have executed this agreement this day of , 19

Kimbell Milling Company d/b/a
Kimbell Grocery Company
(Secured Party)

By T. D. Kidwell

O. K. Supermarkets, Inc.

By: Harold L. Kindle
Vice President
(Debtor)

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FURTHER AGREEMENTS AND WARRANTIES ON THE PART OF THE DEBTOR

Debtor warrants that its title to the Collateral will be good and free of any liens or outstanding interests except the security interest created by this agreement.

Without the prior written consent of the Secured Party which Collateral is fixtures, and, or, equipment Debtor will not sell, exchange, lease or otherwise dispose of the Collateral, or any Debtor's interest therein, and will permit no other lien or security interest to attach to the collateral.

Debtor will maintain the collateral in good condition and repair, but without permitting any repairman's lien to attach thereto. Debtor will pay all taxes and assessments imposed upon the Collateral.

Debtor will carry insurance upon the collateral in such amounts, against such hazards, with such insurers and under such form of policies as may be acceptable to, or requested by, the Secured Party; the insurance policies in every instance to carry a mortgage clause in favor of the Secured Party upon such forms as may be approved by it.

When Collateral is fixtures, and, or, equipment Debtor will not permit the Collateral to be removed from its present location as specified herein, except for temporary periods in the normal and customary use hereof, without the prior written consent of the Secured Party. Collateral consisting of goods, wares and merchandise may be sold in the ordinary course of business, but proceeds claimed by Secured Party. Secured Party may inspect the collateral at any time.

Debtor will pay all costs of filing any financing, continuation or termination statements with respect to the security interest created by this agreement; and the Secured Party is hereby appointed Debtor's attorney in fact to do all acts and things which Secured Party may deem necessary to perfect and continue perfected the security interest created by this agreement and to protect the Collateral. No waiver by Secured Party of any default shall operate as a waiver of any other default or of the same default on a future occasion.

All sums at any time expended by the Secured Party for the protection or preservation of the collateral, or of Secured Party's interest therein shall be repayable by Debtor to Secured Party with interest at the rate of 8% per annum; and such repayment shall be secured by the security interest created herein.

If total or partial default is made in the payment at maturity of any sum (principal or interest) at any time secured hereby; or if default is made in the performance of any obligation imposed upon Debtor hereunder; or if any of the representations or warranties of Debtor made in connection with this transaction shall prove to be false; or if any proceeding is instituted by or against the Debtor under the provisions of the Bankruptcy Act or any state insolvency law or in the event of death of Debtor, or if the Secured Party shall at any time deem its rights hereunder insecure — then, in any of such events, the holders of this security interest may at its option declare all indebtedness secured hereby (with all interest accrued thereon) to be immediately due and payable. In such event, the Secured Party may enforce all remedies available to it under the Uniform Commercial Code.

If the Debtor consists of more than one person the liability hereunder is joint and several and all obligations of Debtor shall bind his heirs, executors or administrators or his or its successors or assigns. All rights of the Secured Party will inure to its successors and assigns.

CORPORATION ACKNOWLEDGMENT

THE STATE OF TEXAS,

COUNTY OF DALLAS

BEFORE ME, the undersigned, a Notary Public in and for said County and State, on this day personally appeared

Harold Kimble

known to me to be the person and officer whose name is subscribed to the foregoing instrument and acknowledged to me that the same was the act of the said

O. K. Supermarkets, Inc.

a corporation, and that he executed the same as the act of such corporation for the purposes and consideration therein expressed, and in the capacity therein stated.

GIVEN UNDER MY HAND AND SEAL OF OFFICE this the 18 day of April A. D. 19 68

(L. S.)

Notary Public in and for Dallas County, Texas.

---

said corporation, and further stated [illegible] the consideration, uses and purposes therein mentioned and set forth.

In testimony whereof I have hereunto set my hand and official seal this 18th day of April, 1968

My Commission expires June 1, 1969

Notary Public

(Notarial Seal)

File No. ____

SECURITY AGREEMENT
AND
FINANCING STATEMENT

STATE OF ____ } ss.
County of ____

I hereby certify that this instrument was filed for record on the ____ day of ____, A.D. 19____, at ____ o'clock ____ M.

____ Clerk

By ____ Deputy

____ Secretary of State

By ____ Deputy

EXHIBIT C

FILING OFFICE COPY — UCC-2[illegible]

4. Maturity Date (if any):

1. Debtor

O K Super Markets
1903 S Ervay
Dallas Texas

2. Secured Party

Kimbell Milling Co
dba Kimbell Gro Co
Ft Worth Texas

3. For Filing Officer

County Clerk

Assignee

☐ Nonstandard Form _____

☐ See Oversize File No. _____

☐ Cross Reference. See:

(2) Acknowledgment

STANDARD FORM—FORM UCC-21—Approved by the Secretary of State of Texas—Form 1568—The Steck Company, Austin, Texas

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[illegible]NG OFFICE COPY - UCC-2[illegible]

4. Maturity Date (if an[illegible])

1. Debtor

O. K. Super Markets, Inc.
1903 South Ervay
Dallas, Texas

2. Secured Party

Kimbell Milling Company
D/B/A
Kimbell Grocery Company
P. O. Box 1540
Fort Worth, Texas 76101

3. For Filing Officer

SECRETARY OF STATE
FILED 8:30 AM

Assignee

Nov 21 83 234990

☒ Nonstandard Form F. S.

☒ See Oversize File No. 0-17019

☐ Cross Reference. See:

(2) FILING OFFICER COPY - ACKNOWLEDGEMENT

STANDARD FORM UCC-21 — Approved by the Secretary of State of Texas

22

SECURITY AGREEMENT AND FINANCING STATEMENT

November 7, 1968
(Date)

O. K. Super Markets, Inc., 1903 South Ervay, Dallas, Texas
(Name) (No. and Street) (City) (State)

(hereinafter called "Debtor", whether one or more), for a valuable consideration hereby acknowledged, hereby grant(s) to

Kimbell Milling Company d/b/a Kimbell Grocery Company
(Name) (No. and Street) (City) (State)

(hereinafter called "Secured Party"), a security interest in the following property and any and all additions and accessions thereto (hereinafter called the "Collateral"): List attached hereto and made a part hereof: ... as additional

O K [illegible]
... SUPER MARKETS, INC.
1903 South Ervay Street
Dallas, Texas 75215

Collateral located at 912 Corinth Street (O K #11)

1-Brunner Belt driven compressor 2 hp. #56A00663R
1-Copelematic 1 hp. #61C13610
1-Copelmatic 1 hp. #09117021
1-Copelmatic 1½hp. #49C051
1-Rheem Central Air Cond. and heating 0051
1-Iron Clad trash pen
1-Iron Clad Bottle shed and storage
XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX
1-8' Beverage Air cold drink box
1-section 3'x8' oil shelves and 1-3' Gondola section and two special shelves
 over cold drinks
24' adjustable gondolas
30' wall shelving adjustable
1-30' reflector mirror
2-Krack coils 1 hp. each
13-metal trays
4-meat lugs
2-sections shelving for cooler
4-meat carts
2-fire extinguishers
1-8' section Tyler 5 deck produce case #499898
1-8' Sheaffer frozen food box with 4 tier shelves
1-two wheeler
1-Toledo produce scale #31699
1-Monroe Sweda register #3440-210885
1-Monroe Sweda register #0308-103355
1-Money order drawer (lock type)
1-12'x3'x12' special drug rack (glass)
1-Hobart meat scale (1.25 chart
1-Dary adding machine
1-3/4 hp. Enterprise grinder #A15654
1-Globe Meat Slicer, stainless steel #169559
1-Meat block
Assorted knives, cleavers, ladles, etc.
1-10' section Tyler meat case with shelves #499906
1-30"x40" Galvanized sink
1-Diebold floor safe "B" Class lid, 2 comp.
1-Formica covered special check-out stand
1-30 cup General Electric Coffee maker
Refrigeration parts, supplies, XXXXXXXXXXXXXXX; all compressors roof-mounted

All other furniture and equipment and accessions. All goods, wares and merchandise and accessions. All accounts and accessions.

Harold Kindle

[signature]

SECURITY AGREEMENT AND FINANCING STATEMENT

November 7, 1968
(Date)

O. K. Super Markets, Inc., 1993 South Ervay, Dallas, Texas
(Name) (No. and Street) (City) (State)

(hereinafter called "Debtor", whether one or more), for a valuable consideration hereby acknowledged, hereby grant(s) to

Kimbell Milling Company d/b/a Kimbell Grocery Company
(Name) (No. and Street) (City) (State)

(hereinafter called "Secured Party"), a security interest in the following property and any and all additions and accessions thereto (hereinafter called the "Collateral"). List attached hereto and made a part hereof:

This Security Agreement and Financing Statement is given as additional security for the Note shown below and it is understood and agreed that this lien is cumulative of all other liens heretofore given to secure this debt and all prior liens shall remain in full force and effect.

to secure payment of a Promissory Note dated April 17, 1968 in the sum of $ 27,000.00, and all extensions and renewals thereof; said security interest also being given to secure the payment of all other indebtedness at any time hereafter owing by Debtor to Secured Party as well as the discharge of all obligations imposed upon Debtor hereunder. If this contract after default is placed in the hands of an attorney, the Debtor will pay the Secured Party a reasonable attorney's fee not exceeding 10% of the unpaid principal and interest, such payment to be secured by the Security Interest herein created.

Debtor further agrees and warrants:

(a) The Collateral is bought or used primarily for: ( ) Personal, family or household purposes; ( ) Farming operations; (X) For use in the operation of a business or profession. If checked here ( ), the collateral is being acquired, in whole or in part, with the proceeds of the above mentioned advance; and the Secured Party is authorized to make such advance direct to the seller.

(b) The Collateral will be kept at 912 Corinth Street, Dallas, Texas
(Street Address) (City) (State)

or if the last preceding space is left blank, it will be kept at the address shown at the beginning of this agreement.

(c) If the collateral is bought or used primarily for business use, the Debtor maintains a place of business at the address shown at the beginning of this Agreement; and all other places of business (if any) of Debtor are located as follows:

List attached and marked Exhibit "A"
(if no other places of business insert "None")

(d) If the Collateral is to be attached to real estate, a description of the real estate is as follows:

NOT APPLICABLE
(If not attached to real estate, insert "NOT APPLICABLE")

and the name of the record owner is

If the Collateral is attached to real estate prior to the perfection of the security interest granted hereby, Debtor will on demand of Secured Party furnish the latter with a disclaimer or disclaimers, signed by all persons having an interest in the real estate, of any interest in the Collateral which is prior to Secured Party's interest.

THIS AGREEMENT IS SUBJECT TO THE ADDITIONAL PROVISIONS SET FORTH ON THE REVERSE SIDE HEREOF, THE SAME BEING INCORPORATED HEREIN BY REFERENCE.

IN WITNESS WHEREOF, the parties hereto have executed this agreement this 14th day of November, 1968

Kimbell Milling Company

d/b/a Kimbell Grocery Company
(Secured Party)

By W. R. Kimbell

O. K. Super Markets, Inc.

By: Harold Kindle
Debtor

President

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OF THE DEBTOR

of any liens or outstanding interests except the security interest created by this agreement, without the prior written consent of Secured Party, when Collateral is fixtures, and, or, equipment Debtor will not [illegible] lease, use or otherwise dispose of the Collateral, or of Debtor's interest therein, and will permit no other lien or security interest to attach to the collateral.

Debtor will keep the collateral in good condition and repair, but without permitting any repairman's lien to attach thereto. Debtor will pay all taxes and assessments imposed upon the Collateral.

Debtor will carry insurance upon the collateral in such amounts, against such hazards, with such insurers and under such form of policies as may be acceptable to, or requested by, the Secured Party; the insurance policies in every instance to carry a mortgage clause in favor of the Secured Party upon such forms as may be approved by it.

When Collateral is fixtures, and, or, equipment Debtor will not permit the Collateral to be removed from its present location as specified herein, except for temporary periods in the normal and customary use hereof, without the prior written consent of the Secured Party. Collateral consisting of goods, wares and merchandise may be sold in the ordinary course of business, but proceeds claimed by Secured Party. Secured Party may inspect the collateral at any time.

Debtor will pay all costs of filing any financing, continuation or termination statements with respect to the security interest created by this agreement; and the Secured Party is hereby appointed Debtor's attorney in fact to do all acts and things which Secured Party may deem necessary to perfect and continue perfected the security interest created by this agreement and to protect the Collateral. No waiver by Secured Party of any default shall operate as a waiver of any other default or of the same default on a future occasion.

All sums at any time expended by the Secured Party for the protection or preservation of the collateral, or of Secured Party's interest therein shall be repayable by Debtor to Secured Party with interest at the rate of 8% per annum; and such repayment shall be secured by the security interest created herein.

If total or partial default is made in the payment at maturity of any sum (principal or interest) at any time secured hereby; or if default is made in the performance of any obligation imposed upon Debtor hereunder; or if any of the representations or warranties of Debtor made in connection with this transaction shall prove to be false; or if any proceeding is instituted by or against the Debtor under the provisions of the Bankruptcy Act or any state insolvency law or in the event of death of Debtor, or if the Secured Party shall at any time deem its rights hereunder insecure -- then, in any of such events, the holders of this security interest may at its option declare all indebtedness secured hereby (with all interest accrued thereon) to be immediately due and payable. In such event, the Secured Party may enforce all remedies available to it under the Uniform Commercial Code.

If the Debtor consists of more than one person the liability hereunder is joint and several and all obligations of Debtor shall bind his heirs, executors or administrators or his or its successors or assigns. All rights of the Secured Party will inure to its successors and assigns.

CORPORATION ACKNOWLEDGMENT

THE STATE OF TEXAS, }

COUNTY OF DALLAS }

BEFORE ME, the undersigned, a Notary Public in and for said County and State, on this day personally appeared

Harold Kindle President, known to me to be the person and officer whose name is subscribed to the foregoing instrument and acknowledged to me that the same was the act of the said

O. K. Super Markets, Inc.

a corporation, and that he executed the same as the act of such corporation for the purposes and consideration therein expressed, and in the capacity therein stated.

GIVEN UNDER MY HAND AND SEAL OF OFFICE this the 14th day of November A. D. 1968.

(L. S.)

Gradath R. Heath

Notary Public in and for Dallas County, Texas.

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the consideration, uses and purposes therein mentioned and set forth.

In testimony whereof I have hereunto set my hand and official seal this 14th day of November 1968

My Commission expires 6-1-69

Notary Public

(Notarial Seal)

File No. ____

SECURITY AGREEMENT
AND
FINANCING STATEMENT

STATE OF ____ } ss.
County of ____ }

I hereby certify that this instrument was filed for record on the ____ day of ____, A.D., 19__, at ____ o'clock ____ M.

____ Clerk

By ____ Deputy

____ Secretary of State

By ____ Deputy

EXHIBIT D

This Financing Statement is presented to a Filing Officer for filing pursuant to the Uniform Commercial Code

3. Maturity Date (if any):

1. Debtor(s) (Last name first) and Mailing Address:

O.K. Supermarkets, Inc.
1903 South Ervay
Dallas, Texas 75215

2. Secured Party(ies) Name and Address:

Republic Nat'l Bank of Dallas
Pacific & Ervay
Dallas, Texas

4. For Filing Officer (Date, Time, Number and Filing Office):

5. This Financing Statement covers the following types (or items) of collateral (If collateral is crops growing or to be grown or goods which are or are to become fixtures, also describe real estate concerned):

All of Debtor's inventory now existing or hereafter acquired, all replacements or substitutes therefor, all accessions, attachments & additions to said inventory, and all similar property hereafter acquired by Debtor, including but not limited to those inventories of groceries and household supplies located at the following premises where Debtor operates a retail grocery chain in Dallas, Texas. 4123 South Oakland, 4630 Hatcher, 1903 S. Ervay, [illegible] Ledbetter, 3029 Grand, 5109 Bexar, 4127 Colonial, 3227 Pennsylvania, 912 Cornich St., Rd., 2900 So. Lamar, 3807 Kiest Blvd.

6. Name and Address of Assignee of Secured Party: (Use this space to describe collateral, if needed)

AUG 7 68 2 0 0 3 5 6

Check [X] if covered: [ ] Proceeds of collateral are also covered. [ ] Products of collateral are also covered. Number of additional sheets presented

7. This Statement is filed without the Debtor's signature to perfect a security interest in collateral
(Please check appropriate box)
- [ ] already subject to a security interest in another jurisdiction when it was brought into this state, or
- [ ] which is proceeds of the original collateral described above in which a security interest was perfected, or
- [ ] already subject to a financing statement filed in another county.

O.K. Supermarkets, Inc.

By _____
Signature(s) of Debtor(s)
President

Republic National Bank of Dallas

By _____
Signature(s) of Secured Party(ies)
Vice-President

(1) Filing Officer Copy—Numerical

STANDARD FORM—FORM UCC-1—APPROVED BY SECRETARY OF STATE OF TEXAS—THE COPE COMPANY, DALLAS, TEXAS 75222

EXHIBIT I

IN THE DISTRICT COURT
TARRANT COUNTY, TEXAS
96TH JUDICIAL DISTRICT

No. 96-5548-70

KIMBELL FOODS, INC., A Corporation, d/b/a KIMBELL MILLING COMPANY, KIMBELL GROCERY COMPANY, AND KIMBELL FORT WORTH COMPANY

vs.

O. K. SUPER MARKETS, INC., A Corporation, JOE F. ELSTON, HAROLD KINDLE, AND GLENN KINDLE, Jointly and Severally, and REPUBLIC NATIONAL BANK OF DALLAS, Jointly and Severally

JUDGMENT

On the 31st day of January, A.D. 1972, came on to be heard the above entitled and numbered cause, and came the Plaintiff by and through its attorneys of record and announced ready for trial, and the Defendants though having answered herein and having been given proper notice of trial, came not, and no jury having been demanded, all matters of fact as well as of law were submitted to the Court, and the Court, after having heard the pleadings, the evidence and arguments of counsel thereon, is of the opinion and finds that Plaintiff's cause of action is liquidated and proven by three Security Agreements, a verified account and guarantees in writing and is entitled to recover judgment against the Defendants for their debt in the amount of $18,258.57 principal, $1,186.80 interest, and reasonable statutory attorneys' fees as against the individual Defendant, O. K. SUPER MARKETS, INC., A CORPORATION, in the sum of $5,000.00, and reasonable contractual attorneys' fees against the individual Defendants, JOE F. ELSTON, HAROLD KINDLE, AND GLENN KINDLE, JOINTLY

AND SEVERALLY, in the sum of $1,825.85, or a total of $24,445.37 as against the individual Defendant, O. K. SUPER MARKETS, INC., A CORPORATION, and a total of $21,271.22 as against the individual Defendants, JOE F. ELSTON, HAROLD KINDLE, AND GLENN KINDLE, JOINTLY AND SEVERALLY. Said judgment to carry joint and several liability as to all Defendants for the sum of $18,258.57 principal, $1,186.80 interest or a total of $19,445.37, together with all costs of Court.

And the Court is further of the opinion and finds that Plaintiff has valid and subsisting security interests as of August 4, 1966, April 17, 1968, and November 7, 1968, in and against any and all property of the Defendant, O. K. SUPER MARKETS, INC., A CORPORATION, as is fully described in said Security Agreements of even date, copies of which are attached hereto and marked Exhibit "A" and referred to herein as if same were set out herein at length, and Plaintiff is entitled to foreclosure of its security interests to satisfy such amounts and costs.

IT IS, THEREFORE, ORDERED, ADJUDGED and DECREED by the Court that the Plaintiff, KIMBELL FOODS, INC., A CORPORATION, D/B/A KIMBELL MILLING COMPANY, KIMBELL GROCERY COMPANY, AND KIMBELL FORT WORTH COMPANY, do have and recover of and from the Defendants, O. K. SUPER MARKETS, INC., A CORPORATION, JOE F. ELSTON, HAROLD KINDLE, AND GLENN KINDLE, JOINTLY AND SEVERALLY, judgment in the sum of $18,258.57 principal, $1,186.80 interest, and reasonable statutory attorneys' fees as against the individual Defendant, O. K. SUPER MARKETS, INC., A CORPORATION, in the sum of $5,000.00, and reasonable contractual attorneys' fees against the individual Defendants, JOE F. ELSTON, HAROLD KINDLE, AND GLENN KINDLE, JOINTLY AND SEVERALLY, in the sum of $1,825.85, or a total of $24,445.37 as against the individual Defendant, O. K. SUPER MARKETS, INC., A CORPORATION, and a total of $21,271.22 as against the individual Defendants, JOE F. ELSTON,

HAROLD KINDLE, AND GLENN KINDLE, JOINTLY AND SEVERALLY. Said judgment to carry joint and several liability as to all Defendants for the sum of $18,258.57 principal, $1,186.80 interest or a total of $19,445.37, together with interest thereon at the rate of six per cent per annum from date hereof, and for all costs of Court.

IT IS FURTHER ORDERED, ADJUDGED and DECREED by the Court that the Plaintiff, KIMBELL FOODS, INC., A CORPORATION, D/B/A KIMBELL MILLING COMPANY, KIMBELL GROCERY COMPANY, AND KIMBELL FORT WORTH COMPANY, do have and is hereby granted foreclosure of its security interests as same existed on August 4, 1966, April 17, 1968, and November 7, 1968, in and to all property as is reflected in the three Security Agreements, copies of which are attached hereto and marked Exhibit "A", and further that an Order of Sale shall issue to the Sheriff or Constable of any County in the State of Texas directing him to seize and sell such property under execution in satisfaction of the indebtedness found against same being the total sum of $24,445.37, and execution shall issue to satisfy the indebtedness and if the property cannot be found or the proceeds of such sale be insufficient to satisfy such indebtedness together with all costs of Court, to make the money or any balance thereof remaining unpaid out of any other property of the Defendants for the amounts due from each Defendant as herein specified, as in the case of ordinary executions and that all other executions are proper for the complete enforcement and satisfaction of this judgment issued herein.

SIGNED this 4th day of February, A.D. 1972.

/s/ [Illegible]
Judge Presiding

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

[Caption Omitted]

[Filed May 24, 1972]

ORIGINAL ANSWER OF DEFENDANT,
REPUBLIC NATIONAL BANK OF DALLAS

TO THE HONORABLE UNITED STATES DISTRICT COURT:

NOW COMES Republic National Bank of Dallas, one of the defendants in the above styled and numbered cause, and in reply to plaintiff's original complaint filed herein, files this its original answer in response thereto, respectfully showing the Court the following:

I.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegation contained in ¶ I regarding jurisdiction.

II.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegation contained in the first sentence of ¶ II. This defendant admits the allegation contained in the second sentence of ¶ II. This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in the third and fourth sentences of ¶ II regarding service on the United States of America.

III.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in ¶ III.

IV.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in ¶ IV.

V.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in ¶ V.

VI.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in ¶ VI.

VII.

This defendant admits the allegations contained in the first and second sentences of ¶ VII. This defendant denies the allegations contained in the last sentence of ¶ VII.

VIII.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in ¶ VIII.

IX.

This defendant denies the allegations contained in ¶ IX.

X.

This defendant admits the sale to Pat H. Hood as alleged in ¶ X, but denies that such sale involved any collateral of the plaintiff.

XI.

This defendant admits the sale to Grand City Groceries, Inc., alleged in ¶ XI, but denies that such sale involved any collateral of the plaintiff.

XII.

This defendant admits the sale to Charles W. Logan alleged in ¶ XII, but denies that such sale involved any collateral of plaintiff.

XIII.

This defendant admits the allegations contained in ¶ XIII.

XIV.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in ¶ XIV.

XV.

This defendant admits that it has refused to pay the plaintiff's alleged claim, but denies all other allegations contained in ¶ XV.

XVI.

This defendant admits the allegations contained in ¶ XVI.

XVII.

This defendant denies the allegations contained in ¶ XVII.

XVIII.

This defendant denies that plaintiff is entitled to the relief sought in the prayer.

XIX.

Further answering, this defendant says that in the amended cause of action filed in the State Court in Tarrant County, Texas, the plaintiff seeks recovery of its account in the sum of $18,258.57 for goods, wares and merchandise sold to defendant O. K. Super Markets, Inc.'s stores from July 1, 1970, through January 13, 1971. That on February 12, 1969, Republic National Bank of Dallas made a loan to O. K. Super Markets, Inc., of $300,000, and out of this sum of money paid to plaintiff $24,893.10, and in consideration for said payment, it was agreed and understood between the parties, Kimbell Foods, Inc., and Republic National Bank of Dallas, that Republic National Bank of Dallas was paying in full all open accounts owed by O. K. Super Markets, Inc., to Kimbell Foods, Inc., and all other indebtednss then

existing between Kimbell Foods, Inc., and O. K. Super Markets, Inc., and that plaintiff agreed to release all financing statements and security agreements then existing between plaintiff and O. K. Super Markets, Inc., so that the financing statement executed by O. K. Super Markets, Inc., in favor of Republic National Bank of Dallas at the time the loan was made would be prior in right and superior over those previously held by plaintiff, and therefore, plaintiff has no right to any of the proceeds realized from the sales referred to in the plaintiff's original complaint, said proceeds being far less than the debt now owing to defendants.

WHEREFORE, PREMISES CONSIDERED, this defendant prays that the plaintiff be denied all relief sought in its complaint with respect to its claim that its security interest in the property of O. K. Super Markets, Inc., is prior and superior to the security interest of defendant Republic National Bank of Dallas, and that it is entitled to judgment in the sum of $24,445.37 against this defendant, and this defendant prays for recovery of its costs, and for such other and further relief which may be proper in the premises.

Respectfully submitted,

GARDERE, PORTER & DEHAY
1700 Republic National Bank Bldg.
Dallas, Texas 75201

By /s/ Frank Betancourt
FRANK BETANCOURT
Attorneys for Defendant
Republic National Bank of Dallas

CERTIFICATE OF SERVICE

I do hereby certify that a copy of the above and foregoing answer was mailed this 24th day of May, 1972, to Mr. Vernon O. Teofan, 820 United Fidelity Bldg., Dallas, Texas 75202, attorney for plaintiff.

/s/ Frank Betancourt
FRANK BETANCOURT

IN THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF TEXAS DALLAS DIVISION

[Caption Omitted]

[Filed July 5, 1972]

ORIGINAL ANSWER OF DEFENDANT, UNITED STATES OF AMERICA

TO THE HONORABLE JUDGE OF SAID COURT:

NOW COMES United States of America, by and through Eldon B. Mahon, United States Attorney for the Northern District of Texas, and Charles D. Cabaniss, Assistant United States Attorney in and for said District, one of the defendants in the above styled and numbered cause, and in reply to plaintiff's original complaint filed herein, files this its original answer in response thereto, respectfully showing the Court the following:

I.

This defendant admits the allegation contained in paragraph I regarding jurisdiction.

II.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegation contained in the first sentence of paragraph II. This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in the second and fourth sentences of paragraph II regarding service on the Republic National Bank of Dallas. This Defendant admits the allegation contained in the third and fourth sentences of paragraph II.

III.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph III.

IV.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph IV.

V.

The defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph V.

VI.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph VI.

VII.

This defendant admits the allegations contained in the first and second sentences of paragraph VII. This defendant denies the allegations contained in the last sentence of paragraph VII.

VIII.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph VIII.

IX.

This defendant denies the allegations contained in paragraph IX.

X.

This defendant admits the sale to Pat H. Hood as alleged in paragraph X, but denies that such sale involved any collateral of the plaintiff.

XI.

This defendant admits the sale to Grand City Groceries, Inc., alleged in paragraph XI, but denies that such sale involved any collateral of the plaintiff.

XII.

This defendant admits the sale to Charles W. Logan alleged in paragraph XII, but denies that such sale involved any collateral of plaintiff.

XIII.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph XIII.

XIV.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph XIV.

XV.

This defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph XV.

XVI.

This defendant admits the allegations contained in paragraph XVI.

XVII.

This defendant denies the allegations contained in paragraph XVII.

XVIII.

This defendant denies that plaintiff is entitled to the relief sought in the prayer.

XIX.

Further answering, this defendant says that on February 12, 1969, Republic National Bank of Dallas made a loan to O.K. Super Markets, Inc., of $300,000, and out of this sum of money paid to plaintiff $24,893.10, and in consideration for said payment, it was agreed and understood between the parties, Kimbell Foods, Inc., and Repub-

lic National Bank of Dallas, that Republic National Bank of Dallas was paying in full all open accounts owed by O.K. Super Markets, Inc., to Kimbell Foods, Inc., and all other indebtedness then existing between Kimbell Foods, Inc., and O.K. Super Markets, Inc., and that plaintiff agreed to release all financing statements and security agreements then existing between plaintiff and O.K. Super Markets, Inc., so that the financing statement executed by O.K. Super Markets, Inc., in favor of Republic National Bank of Dallas at the time the loan was made would be prior in right and superior over those previously held by plaintiff, and therefore, plaintiff has no right to any of the proceeds realized from the sales referred to in the plaintiff's original complaint, said proceeds being far less than the debt now owing to the defendants.

WHEREFORE, PREMISES CONSIDERED, this defendant prays that the plaintiff be denied all relief sought in its complaint with respect to its claim that its security interest in the property of O.K. Super Markets, Inc., is prior and superior to the security interest of defendant United States of America, and that it is entitled to judgment in the sum of $24,445.37 against this defendant, and this defendant prays for recovery of its

costs, and for such other and further relief which may be proper in the premises.

Respectfully submitted,
ELDON B. MAHON
United States Attorney

By /s/ Charles D. Cabaniss
CHARLES D. CABANISS
Assistant United States Attorney

CERTIFICATE OF SERVICE

I do hereby certify that a copy of the above and foregoing answer was mailed this 5th day of July, 1972, to Mr. Vernon O. Teofan, 820 United Fidelity Bldg., Dallas, Texas 75202, attorney for plaintiff, and Frank Betancourt, 1700 Republic National Bank Building, Dallas, Texas, attorney for Republic National Bank.

/s/ Charles D. Cabaniss
CHARLES D. CABANISS
Assistant United States Attorney

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
FORT WORTH DIVISION

[Caption Omitted]

[Filed July 13, 1973]

PRE-TRIAL ORDER

A pre-trial conference was held in the above-entitled cause before Honorable Leo Brewster, Judge, on the 26th day of July, 1973. Vernon O. Teofan, Esq. appeared as counsel for Plaintiff, KIMBELL FOODS, INC.; Frank Betancourt, Esq. appeared as counsel for Defendant REPUBLIC NATIONAL BANK OF DALLAS; Claude Brown, Esq. appeared as counsel for the UNITED STATES OF AMERICA; Lewis A. Jones, Esq. appeared as counsel for the Intervenor STATE OF TEXAS and Ted P. MacMaster, Esq. appeared as counsel for the Intervenor CITY OF DALLAS.

1. The following jurisdictional questions were raised and disposed of as hereinafter indicated:

All parties agree and stipulate that this Court has jurisdiction of the causes of action alleged in Plaintiff's complaint, Intervenors' complaint and Defendants' answers.

2. The following disposition was made of pending motions or other similar matters preliminary to trial:

No motions or other similar matters preliminary to trial were pending.

3. In general, the Plaintiff claims:

(1) On or about August 4, 1966, O. K. Super Markets, Inc., for good and valuable consideration, made, executed and delivered to Plaintiff, its Security Agreement and Financing Statement granting Plaintiff a security interest in therein listed equipment and fixtures and in all goods, wares and merchandise and any and all additions or accessions thereto to secure payment of the therein described promissory note and all extensions and renewals thereof and all other indebtedness at any time thereafter owing by O. K. Super Markets, Inc. to Plaintiff as well as the discharge of all obligations imposed on O. K. Super Markets, Inc. thereunder which was filed with the Secretary of State of Texas on September 2, 1966. (Plaintiff's Exhibit "1")

(2) On or about April 17, 1968, said O. K. Super Markets, Inc. for good and valuable consideration, made, executed and delivered to Plaintiff its Security Agreement and Financing Statement granting to Plaintiff a security interest in therein described equipment and in all other furniture, fixtures and equipment, all goods, wares, merchandise and stock in trade and any and all additions and accessions thereto to secure the payment of the therein described promissory note and all extensions and renewals thereof and all other indebtedness at any time thereafter owing by O. K. Super Markets, Inc. to Plaintiff as well as the discharge of all obligations imposed upon O. K. Super Markets, Inc. thereunder which was filed with the Secretary of State of Texas on April 22, 1968. (Plaintiff's Exhibit "2")

(3) On or about November 7, 1968, said O. K. Super Markets, Inc. for good and valuable consideration made, executed and delivered to Plaintiff its Security Agreement and Financing Statement granting to Plaintiff a security interest in therein described equipment and in all goods, wares, merchandise and accounts and any and all additions and accessions thereto to secure the payment of the therein described promissory note and all extensions and renewals thereof and all other indebtedness at any time thereafter owing by O. K. Super Markets, Inc. to Plaintiff as well as the discharge of all obligations imposed upon O. K. Super Markets, Inc. thereunder which was filed with the Secretary of State of Texas on November 21, 1968. (Plaintiff's Exhibit "3")

(4) Said three Security Agreements and Financing Statements were cumulative of each other and the Security Agreements dated April 17, 1968 and November 7, 1968 were in addition and an extension of the Se-

curity Agreement and Financing Statement dated August 4, 1966 and under the laws of the State of Texas, Plaintiff's security interest in the collateral described in said Security Agreements and Financing Statements was duly perfected as of September 2, 1966.

(5) On or about February 3, 1971 an agreement (Plaintiff's Exhibit "7") was entered into by and between O. K. Super Markets, Inc. and Defendant REPUBLIC NATIONAL BANK OF DALLAS and approved as to form and substance by Defendant Small Business Administration and Plaintiff whereunder collateral covered by the Security Agreements and Financing Statements of Plaintiff were to be sold and liquidated with the proceeds thereof to be held in escrow by Defendant REPUBLIC NATIONAL BANK and paid over to the party or parties entitled to same after due adjudication and/or mutual agreement between the parties thereto.

(6) On or about February 8, 1971 collateral covered by the Security Agreements and Financing Statements of Plaintiff was sold and liquidated as follows:

A. Collateral located at O. K. Super Markets, Inc., Store No. 14, 3805 Kiest Boulevard, Dallas, Texas was sold to Pat Hood for the total sum of $30,000.00, $18,000.00 thereof being attributable to the inventory of stock in trade and $12,000.00 thereof to the fixtures, equipment and other property (Plaintiff's Exhibits "8" and "9");

B. Collateral located at O. K. Super Markets, Inc., Store No. 5, 3026 Grand Avenue, Dallas, Texas was sold to Grand City Groceries, Inc. for a total price of $30,000.00, $18,000.00 thereof being attributable to inventory of stock in trade and $12,000.00 thereof to fixtures, equipment and other property (Plaintiff's Exhibits "10' and "11"); and

C. Collateral located at O. K. Super Markets, Inc., Store No. 3, 1903 South Ervay Street, Dallas, Texas was sold to Charles W. Logan for the total price of $35,000.00, $21,000.00 thereof being attributable to the inventory of stock in trade and

$14,000.00 thereof to fixtures, equipment and other property (Plaintiff's Exhibits "12" and "13");

and the proceeds of such sales were deposited with REPUBLIC NATIONAL BANK OF DALLAS under the agreement of February 3, 1971.

(7) O. K. Super Markets, Inc. is indebted to Plaintiff as follows:

A. $18,258.57 principal owing on open account;

B. Interest on said sum from January 1, 1971 until paid at the rate of 6% per annum;

C. Reasonable statutory attorneys' fees in the sum of $5,000.00;

D. All costs incurred in collecting said sums: all of which are secured by Plaintiff's security interests granted in said Security Agreements and Financing Statements.

(8) Plaintiff's security interest in the property of O. K. Super Markets, Inc. sold pursuant to said agreement of February 3, 1971 is prior in time, prior in right and superior to any security interest therein asserted by Defendant REPUBLIC NATIONAL BANK OF DALLAS and its assignee, Defendant Small Business Administration, and Plaintiff is entitled to be paid from the proceeds realized from the sale thereof being held by Defendant REPUBLIC NATIONAL BANK to the extent of the indebtedness due and owing to it by O. K. Super Markets, Inc. as above set forth.

4. In general, the Defendant claims:

(1) On August 7, 1968, O. K. Super Markets, Inc. executed and delivered to REPUBLIC NATIONAL BANK its Financing Statement (Defendants' Exhibit "1") covering all debtor's machinery, fixtures, equipment and inventory then existing or thereafter acquired, all replacements and substitutes thereof, all accessions, attachments and additions thereto, and all tools, parts and equipment then or thereafter added to or used in connection with such machinery and equipment, and all similar property thereafter acquired by debtor to secure the payment of funds loaned by REPUBLIC NATIONAL

BANK to O. K. Super Markets, Inc., 90% of which loan was guaranteed by Small Business Administration of the United States of America which was filed with the Secretary of State of Texas on or about August 7, 1968.

(2) On or about February 12, 1969, O. K. Super Markets, Inc. for good and valuable consideration, made, executed and delivered to Defendant REPUBLIC NATIONAL BANK OF DALLAS, its Security Agreement (Defendants' Exhibit "2") and Financing Statement (Defendants' Exhibit "3") providing for a security interest in all of debtor's machinery, fixtures, equipment and inventory, then existing or thereafter acquired, all replacements and substitutes therefor, all accessions, attachments and additions thereto, and all tools, parts and equipment then or thereafter added to or used in connection with such machinery and equipment, and all similar property thereafter acquired by debtor located at 1403 South Ervay, 4123 South Oakland, 4630 Hatcher, 3805-7 East Kiest Boulevard, 3026 Grand Avenue, 4121 Colonial, R 912 Corinth Street, 2900 South Lamar, 1903-19 South Ervay, 5109 Bexar, 3227 Pennsylvania, all proceeds of, substitutes and replacements for, accessions, attachments and other additions to, and tools, parts and equipment used in connection with the above property, all property similar thereto thereafter acquired by the debtor to secure the obligations therein stated which Financing Statement was filed with the Secretary of State of Texas on February 18, 1969.

(3) On or about February 12, 1969, Defendant REPUBLIC NATIONAL BANK OF DALLAS loaned to said O. K. Super Markets, Inc. the sum of $300,000.00 as evidenced by a promissory note (Defendants' Exhibit "4") dated February 12, 1969, executed by O. K. Super Markets, Inc. and payable to Defendant REPUBLIC NATIONAL BANK OF DALLAS as therein specified.

(4) 90% of said loan from Defendant REPUBLIC NATIONAL BANK OF DALLAS to O. K. Super Markets, Inc. was guaranted by Small Business Administration of the United States of America, as per Blanket

Guaranty Agreement and Application for Loan Under Blanket Guaranty (Defendants' Exhibit "5").

(5) Out of the $300,000.00 loaned by Defendant REPUBLIC NATIONAL BANK OF DALLAS to O. K. Super Markets, Inc. on February 12, 1969, $24,892.10 was paid to Plaintiff, paying in full a promissory note dated April 17, 1968, in original principal sum of $27,-000.00 executed by O. K. Super Markets, Inc., payable to Plaintiff, said $24,893.10 paying principal balance of $24,000.00 and interest $893.10 in full.

(6) As of February 12, 1969, no other outstanding promissory note existed between O. K. Super Markets, Inc. and Plaintiff other than said $27,000.00 note.

(7) In consideration of said payment, it was agreed and understood between Plaintiff KIMBELL FOODS, INC. and Defendant REPUBLIC NATIONAL BANK OF DALLAS, that REPUBLIC NATIONAL BANK OF DALLAS was paying in full all secured indebtedness owed by O. K. Super Markets, Inc. to KIMBELL FOODS, INC.

(8) Plaintiff agreed to release the Security Agreements and Financing Statements then existing between Plaintiff and O. K. Super Markets, Inc. so that the Security Agreement and Financing Statement executed by O. K. Super Markets, Inc. in favor of REPUBLIC NATIONAL BANK OF DALLAS at the time the loan was made would be prior and superior.

(9) On or about February 3, 1971, the Small Business Administration of the United States of America paid to REPUBLIC NATIONAL BANK OF DALLAS 90% of O. K. Super Markets, Inc.'s indebtedness to the REPUBLIC NATIONAL BANK OF DALLAS and was accordingly assigned the security interest held by REPUBLIC NATIONAL BANK OF DALLAS in property of O. K. Super Markets, Inc. described in the Security Agreement and Financing Statement.

(10) The security interest granted in the Financing Statement and Security Agreement in favor of REPUBLIC NATIONAL BANK dated February 12, 1969 is prior in right and superior to those previously held by the Plaintiff.

(11) By paying said $24,893.10 to Plaintiff, REPUBLIC NATIONAL BANK and Small Business Administration became subrogated to such extent to the rights and security interests, if any, of Plaintiff.

5. In general, the Intervenors claim:

Claims of Intervenors are set out in Supplemental Pre-Trial Order.

6. The following facts are established by the pleadings or are established by the stipulations or admissions of counsel:

(1) Plaintiff, KIMBELL FOODS, INC., is a corporation duly incorporated and existing under and by virtue of the laws of the State of Texas, with its principal office and place of business in Fort Worth, Tarrant County, Texas and was formerly known as Kimbell Milling Company and did business as Kimbell Grocery Company.

(2) Defendant, REPUBLIC NATIONAL BANK OF DALLAS, is a national banking corporation, organized under the laws of the United States of America with its principal office and place of business in Dallas, Dallas County, Texas.

(3) Small Business Administration is an agency of Defendant UNITED STATES OF AMERICA.

(4) O. K. Super Markets, Inc. is or was a corporation duly incorporated and existing under and by virtue of the laws of the State of Texas, with its principal offices and place of business in the City of Dallas, County of Dallas and State of Texas.

(5) On or before August 4, 1966, O. K. Super Markets, Inc., for good and valuable consideration, made, executed and delivered to Plaintiff, its Security Agreement and Financing Statement (Plaintiff's Exhibit "1") which was filed with the Secretary of State of Texas on September 2, 1966. No termination statement relating thereto has been executed by Plaintiff or filed with the Secretary of State of Texas.

(6) On or about April 17, 1968, O. K. Super Markets, Inc., for good and valuable consideration, made, executed and delivered to the Plaintiff, its Security Agreement and Financing Statement (Plaintiff's Exhibit "2") which was

filed with the Secretary of State of Texas on April 22, 1968. No termination statement relating thereto has been executed by Plaintiff or filed with the Secretary of State of Texas.

(7) On or about August 7, 1968, O. K. Super Markets, Inc. signed and delivered to REPUBLIC NATIONAL BANK a Financing Statement (Defendants' Exhibit "1") covering the types or items of collateral described in Block 5 thereof which was filed with the Secretary of State of Texas on August 7, 1968. No termination statement relating thereto has been executed by REPUBLIC NATIONAL BANK or the Small Business Administration or filed with the Secretary of State of Texas.

(8) On or about November 7, 1968, O. K. Super Markets, Inc. for good and valuable consideration, made, executed and delivered to the Plaintiff, its Security Agreement and Financing Statement (Plaintiff's Exhibit "3") which was filed with the Secretary of State of Texas on November 21, 1968. No termination statement relating thereto has been executed by Plaintiff or filed with the Secretary of State of Texas.

(9) On February 12, 1969 O. K. Super Markets, Inc. was indebted to Plaintiff in the approximate sum of $24,893.10 on a promissory note (Plaintiff's Exhibit "4") dated April 17, 1968 in the original principal sum of $27,000.00. Marked Plaintiff's Exhibit "5" is a statement reflecting charges and credits to said note. No other outstanding promissory note existed between O. K. Super Markets, Inc. and Plaintiff on February 12, 1969.

(10) On or about February 12, 1969 said O. K. Super Markets, Inc. was additionally indebted to Plaintiff for merchandise sold on open account in the sum of $18,-390.93 and has been continuously indebted on open account to Plaintiff thereafter up to and including the present time. Marked Plaintiff's Exhibit "6" is a statement of the accounts between Plaintiff and O. K. Super Markets, Inc. during the period January 15, 1969 through January 15, 1971.

(11) On or about February 12, 1969, O. K. Super Markets, Inc. for good and valuable consideration made, executed and delivered to Defendant REPUBLIC NA-

TIONAL BANK OF DALLAS, its Security Agreement (Defendants' Exhibit "2") providing for a security interest in the therein described collateral.

(12) On or about February 12, 1969, O. K. Super Markets, Inc. signed and delivered to REPUBLIC NATIONAL BANK OF DALLAS a Financing Statement (Defendants' Exhibit "3") covering the types or items of collateral described in Block 5 thereof which was filed with the Secretary of State of Texas on February 18, 1969. No termination statement relating thereto has been executed by REPUBLIC NATIONAL BANK or the Small Business Administration or filed with the Secretary of State of Texas.

(13) On or about February 12, 1969, Defendant REPUBLIC NATIONAL BANK OF DALLAS loaned to said O. K. Super Markets, Inc. the sum of $300,000.00 as evidenced by a promissory note dated February 12, 1969 executed by O. K. Super Markets, Inc. and payable to Defendant REPUBLIC NATIONAL BANK OF DALLAS as therein specified.

(14) 90% of said loan from Defendant REPUBLIC NATIONAL BANK OF DALLAS to O. K. Super Markets, Inc. was guaranteed by Small Business Administration of the United States of America (Defendants' Exhibit "5").

(15) Out of the $300,000.00 loan by Defendant REPUBLIC NATIONAL BANK OF DALLAS to O. K. Super Markets, Inc. on February 12, 1969 $24,893.10 was paid to Plaintiff and applied by Plaintiff to the payment of balance owing on its promissory note (Plaintiff's Exhibit "4").

(16) As reflected in said Plaintiff's Exhibit "6", subsequent to February 12, 1969, O. K. Super Markets, Inc. paid to Plaintiff a sum in excess of $18,390.93 which was credited by Plaintiff against the oldest outstanding charges on said accounts and the balance now outstanding on said accounts represents charges for merchandise sold by Plaintiff to O. K. Super Markets, Inc. subsequent to February 12, 1969. Marked as Defendants' Exhibit "6" is a statement of the accounts between Plaintiff and O. K.

Super Markets, Inc. during the period July 1, 1970 through January 15, 1971.

(17) After January 15, 1971, Plaintiff transacted no further business with O. K. Super Markets, Inc. and has received no payments from O. K. Super Markets, Inc. on said account and the present principal balance thereof is $18,258.57.

(18) On January 15, 1971, Plaintiff filed suit in the 96th Judicial District Court of Tarrant County, Texas, Cause No. 96-5548-70 against O. K. Super Markets, Inc. and others to recover, among other things, judgment against said O. K. Super Markets, Inc. for its indebtedness to Plaintiff in the amount of $18,258.57 principal, plus interest, reasonable contractual and statutory attorneys' fees, costs of suit and foreclosure of its security interest in the collateral described in its Security Agreements (Plaintiff's Exhibits "1", "2" and "3").

(19) On or about February 3, 1971, an agreement was entered into by and between said O. K. Super Markets, Inc. and Defendant REPUBLIC NATIONAL BANK OF DALLAS and approved as to form and substance by Defendant Small Business Administration of the United States of America and Plaintiff whereunder property of O. K. Super Markets, Inc. located at 3805 Kiest Boulevard, 3026 Grand Avenue and 1903 South Ervay was to be sold and liquidated with the proceeds thereof to be held in escrow by Defendant REPUBLIC NATIONAL BANK OF DALLAS and paid over to the party or parties entitled to same after due adjudication and/or mutual agreement between the parties thereto. Marked Plaintiff's Exhibit "7" is a true and correct copy of said agreement.

(20) On or about February 3, 1971 the Small Business Administration of the United States of America paid to REPUBLIC NATIONAL BANK OF DALLAS 90% of O. K. Super Markets, Inc.'s indebtedness to the REPUBLIC NATIONAL BANK OF DALLAS which was in the amount of $252,331.93 and has accordingly been assigned a proportionate interest in the security interest held by REPUBLIC NATIONAL BANK OF DALLAS in prop-

erty of O. K. Super Markets, Inc. described in the Security Agreement a copy of which is marked Defendants' Exhibit "2". Marked Defendants' Exhibit "7" is a true and correct copy of the Assignment filed with the Secretary of State of Texas on January 21, 1971.

(21) On or about February 8, 1971 the collateral located at O. K. Super Markets, Inc., Store No. 14, 3805 Kiest Boulevard, Dallas, Dallas County, Texas, was sold to Pat H. Hood for the total sum of $30,000.00, $12,000.00 thereof being attributed to the fixtures, equipment and other property and $18,000.00 attributed to inventory of stock in trade. Marked Plaintiff's Exhibit "8" is a true and correct copy of the Contract of Sale under which said collateral was sold to Pat H. Hood. Marked Plaintiff's Exhibit "9" is a true and correct copy of the promissory note executed by Pat Hood referred to in said Contract of Sale.

(22) On or about February 8, 1971 the collateral located at O. K. Super Markets, Inc., Store No. 5, 3026 Grand Avenue, Dallas, Dallas County, Texas, was sold to Grand City Groceries, Inc. for a total price of $30,000.00, $18,000.00 thereof being attributable to the inventory of stock in trade and $12,000.00 thereof to the fixtures, equipment and other property. Marked Plaintiff's Exhibit "10" is a true and correct copy of the Contract of Sale under which said collateral was sold to Grand City Groceries, Inc. Marked Plaintiff's Exhibit "11" is a true and correct copy of the promissory note executed by Grand City Groceries, Inc. referred to in said Contract of Sale.

(23) On or about February 8, 1971, the collateral located at O. K. Super Markets, Inc., Store No. 3, 1903 South Ervay Street, Dallas, Texas, was sold to Charles W. Logan for the total price of $35,000.00, $21,000.00 thereof being attributable to the inventory of stock in trade and $14,000.00 thereof to the fixtures, equipment and other property. Marked Plaintiff's Exhibit "12" is a true and correct copy of the Contract of Sale under which said collateral was sold to Charles W. Logan. Marked Plaintiff's Exhibit "13" is a true and correct copy of the

promissory note executed by Charles W. Logan referred to in said Contract of Sale.

(24) Thereafter by amended petition, REPUBLIC NATIONAL BANK OF DALLAS was made a party Defendant in said Cause No. 96-5548-70 in the 96th Judicial District Court of Tarrant County, Texas and thereafter, said cause as it pertained to said REPUBLIC NATIONAL BANK OF DALLAS was transferred upon the Plea of Privilege of REPUBLIC NATIONAL BANK OF DALLAS to the 134th Judicial District Court of Dallas County, Texas where it remains pending.

(25) On January 31, 1972, judgment was entered in said Cause No. 96-5548-70 in favor of Plaintiff and against O. K. Super Markets, Inc. in the sum of $18,258.57 principal, $1,186.80 interest and reasonable attorneys' fees in the sum of $5,000.00 and granting foreclosure of said security interests as the same existed on August 4, 1966, April 17, 1968 and November 7, 1968 in and to all property as reflected in said three Security Agreements, copies of which are marked Plaintiff's Exhibits "1", "2" and "3". Marked Plaintiff's Exhibit "14" is a true and correct copy of said judgment. Said judgment is final, valid and subsisting and has not been paid in whole or in part.

(26) There is now due and owing Small Business Administration by O. K. Super Markets, Inc. the sum of $252,331.93 plus interest on said $300,000.00 note (Defendants' Exhibit "4").

(27) As of March 15, 1973, REPUBLIC NATIONAL BANK OF DALLAS holds in escrow under said agreement of February 3, 1971 the sum of $86,672.00.

(28) Although due demand has been made by Plaintiff upon said Defendant REPUBLIC NATIONAL BANK OF DALLAS, said bank has wholly failed and refused to pay Plaintiff's claim to said funds.

(29) Although due demand has been made by Plaintiff upon the Small Business Administration, said Small Business Administration has wholly failed and refused to authorize the payment of Plaintiff's claim to said funds.

7. The contested issues of fact are:

(1) Whether or not, in consideration of the payment of $24,893.10 to Plaintiff on or about February 12, 1969, it was agreed and understood between Plaintiff and Defendant REPUBLIC NATIONAL BANK OF DALLAS that REPUBLIC NATIONAL BANK OF DALLAS was paying in full all secured indebtedness owed by O. K. Super Markets, Inc. to KIMBELL FOODS, INC.

(2) Whether or not Plaintiff agreed, expressly or impliedly, with REPUBLIC NATIONAL BANK OF DALLAS to release all Financing Statements and Security Agreements existing on February 12, 1969 between Plaintiff and O. K. Super Markets, Inc. so the Financing Statement and Security Agreement executed by O. K. Super Markets, Inc. in favor of REPUBLIC NATIONAL BANK OF DALLAS at the time the loan was made would be prior in right and superior to the Security Agreements and Financing Statements held by Plaintiff.

(3) What amount would be a reasonable attorneys' fee for the services of the attorneys for the Plaintiff which have been rendered by them in representing the Plaintiff in connection with the collection of its claim against O. K. Super Markets, Inc. and the enforcement of its security interests relating thereto.

(4) Whether or not the Financing Statement (Defendants' Exhibit "1") filed with the Secretary of State on August 7, 1968 was signed and filed for the purpose of perfecting, in whole or in part, the security interest provided for in the Security Agreement dated February 12, 1969 (Defendants' Exhibit "2").

(5) What sums, if any, have been expended, or what costs, if any, have been incurred by the Plaintiff for the protection or preservation of its security interest in the collateral described in its three Security Agreements (Plaintiff's Exhibits "1", "2" and "3").

8. The contested issues of law are:

(1) Whether or not the security interest provided for in the Security Agreement dated February 12, 1969 in favor of REPUBLIC NATIONAL BANK (Defendants'

Exhibit "2") is prior in right and superior to the security interests provided for in the Security Agreement and Financing Statement dated August 4, 1966 (Plaintiff's Exhibit "1"), the Security Agreement and Financing Statement dated April 17, 1968 (Plaintiff's Exhibit "2") or the Security Agreement and Financing Statement dated November 7, 1968 in favor of the Plaintiff.

(2) Whether or not the security interest provided for in the Financing Statements in favor of the Plaintiff (Plaintiff's Exhibits "1", "2", and "3") were extinguished upon the payment to Plaintiff of the outstanding balance due and owing on O. K. Super Markets, Inc.'s promissory note dated April 17, 1968 in the original principal sum of $27,000.00.

(3) Whether or not the security interests provided for in the Security Agreements and Financing Statements in favor of Plaintiff were extinguished when the balance of O. K. Super Markets, Inc.'s open account indebtedness existing as of February 12, 1969 was thereafter paid.

(4) Whether or not the judgment entered in Cause No. 96-5548-70 in the District Court of Tarrant County, Texas 96th Judicial District, establishes or fixes, as against Defendants and Intervenors, the amount of Plaintiff's claim against O. K. Super Markets, Inc. secured by the security interests provided for in the Security Agreements and Financing Statements in favor of Plaintiff.

(5) Whether or not Plaintiff is entitled to recover attorneys' fees as against O. K. Super Markets, Inc. which are secured by the security interests provided for in the Security Agreements and Financing Statements in favor of Plaintiff.

(6) Whether or not the security interests provided for in the Security Agreements and Financing Statements in favor of Plaintiff securing the payment of such attorneys' fees are prior in right and superior to the security interests provided for in the Security Agreement in favor of REPUBLIC NATIONAL BANK OF DALLAS.

(7) Whether or not the security interest provided for in the Security Agreement in favor of REPUBLIC NATIONAL BANK dated February 12, 1969 (Defendants' Exhibit "2") is perfected, in whole or in part, by the

Financing Statement filed with the Secretary of State on August 7, 1968 (Defendants' Exhibit "1").

(8) Whether or not the Plaintiff is a party to or a beneficiary under the agreement of February 3, 1971 entered into by and between O. K. Super Markets, Inc. and REPUBLIC NATIONAL BANK OF DALLAS and approved as to form and substance by Small Business Administration and Plaintiff (Plaintiff's Exhibit "7").

(9) Whether or not the security interests provided for in the Security Agreements in favor of the Plaintiff (Plaintiff's Exhibits "1", "2" and "3") securing the repayment of sums expended or costs incurred by the Plaintiff for the protection or preservation of its security interest in the collateral described in said Security Agreements is prior in right and superior to the security interest provided for in the Security Agreement in favor of REPUBLIC NATIONAL BANK (Defendants' Exhibit "2").

(10) Whether or not REPUBLIC NATIONAL BANK and the Small Business Administration are subrogated to the claims and security interests of Plaintiff, if any, by reason of the payment to Plaintiff of said $24,893.10 on or about February 12, 1969.

9. The following exhibits were marked:

A. Plaintiff's Exhibits

1. Security Agreement and Financing Statement dated August 4, 1966 with Filing Office Copy—UCC-21 attached.

2. Security Agreement and Financing Statement dated April 17, 1968 with Filing Office Copies—UCC-21's attached.

3. Security Agreement and Financing Statement dated November 7, 1968 with Filing Office Copies—UCC-21's attached.

4. Copy of note dated 4/17/68 in the original principal sum of $27,000.00 executed by O. K. Super Markets, Inc. and payable to Plaintiff.

5. Statement relating to promissory note of O. K. Super Markets, Inc. to Plaintiff dated 4/17/68 in the original principal sum of $27,000.00.

6. Statements of account between Plaintiff and O. K. Super Markets, Inc. covering the period January 15, 1969 through January 15, 1971.

7. Agreement dated February 3, 1971 between O. K. Super Markets, Inc. and Republic National Bank and approved as to form and substance by Small Business Administration and Kimbell Foods, Inc.

8. Contract of Sale dated February, 1971 between O. K. Super Markets, Inc. and Pat H. Hood.

9. Installment promissory note dated February 8, 1971 in the principal sum of $25,000.00 executed by Pat H. Hood and payable to Republic National Bank of Dallas (Escrow Agent).

10. Contract of Sale dated February 8, 1971 between O. K. Super Markets, Inc. and Grand City Groceries, Inc.

11. Installment promissory note dated February 18, 1970 in the principal sum of $25,000.00 executed by Grand City Groceries, Inc. and payable to Republic National Bank of Dallas (Escrow Agent).

12. Contract of Sale dated February 8, 1971 between O. K. Super Markets, Inc. and Charles W. Logan.

13. Installment promissory note dated February 8, 1971 in the principal sum of $30,000.00 executed by Charles W. Logan payable to Republic National Bank of Dallas (Escrow Agent).

14. Judgment entered in Cause No. 96-5548-70 in the 96th Judicial District Court of Tarrant County, Texas on February 4, 1972.

15. Bill of Sale dated February 8, 1971 from O. K. Super Markets, Inc. to Pat H. Hood.

16. Bill of Sale dated February 8, 1971 from O. K. Super Markets, Inc. to Grand City Groceries, Inc.

17. Bill of Sale dated February 8, 1971 from O. K. Super Markets, Inc. to Charles W. Logan.

18. Memo from M. D. Kidwell dated 11/12/68.

19. Intercompany and office correspondence dated November 19, 1968 to Mr. W. E. Hartman from M. D. Kidwell.

20. Intercompany and office correspondence dated November 26, 1968 to Mr. W. E. Hartman from M. D. Kidwell.

21. Intercompany and office correspondence dated January 16, 1969 to Mr. W. E. Hartman from M. D. Kidwell and attachments.

B. Defendants' Exhibits

1. Financing Statement filed with Secretary of State on August 7, 1968 bearing number 206396.

2. Security Agreement dated February 12, 1969 wherein Republic National Bank of Dallas is bank and O. K. Super Markets, Inc. is debtor.

3. Financing Statement filed with Secretary of State on February 18, 1969 bearing number 254984.

4. Promissory note dated February 12, 1969 in the principal sum of $300,000.00 executed by O. K. Super Markets, Inc. payable to the order of Republic National Bank with assignment to Small Business Administration attached.

5. Small Business Administration Application for Loan under Blanket Guaranty SBA Loan No. SBLG-ME-752,344-00-04-DAL dated January 8, 1969 and Blanket Loan Guaranty Agreement between Small Business Administration and Republic National Bank dated November 1, 1967.

6. Statement of account between Plaintiff and O. K. Super Markets, Inc. covering the period July 1, 1970 through January 15, 1971.

7. Assignment filed with Secretary of State of Texas on February 18, 1971.

8. Check from Republic National Bank to Plaintiff in the sum of $24,893.10.

9. Loan authorization between Republic National Bank, O. K. Super Markets, Inc. and the Small Business Administration.

10. The following expert witnesses will be called by the parties:

None

11. A general statement of suggested instructions to the jury by the parties, respectively, are:

Not applicable. No party has requested trial by jury.

12. The following amendments to the pleadings are requested:

(1) Plaintiff requests leave of Court to amend its complaint filed herein by substituting for the presently attached Exhibit "E" a copy of the agreement between O. K. Super Markets, Inc. and the REPUBLIC NATIONAL BANK OF DALLAS approved as to form and substance by Small Business Administration and Plaintiff as actually executed (Plaintiff's Exhibit "7") and substituting for the following wording contained in paragraph IX thereof:

> "Pending a resolution of the above-referred to cause of action No. 96-5548-70 filed in the 96th Judicial District Court of Tarrant County, Texas and to be paid over to the party or parties in the manner and amounts as finally determined to be legal and rightful,"

the words: "to be paid over to the party or parties entitled to same after due adjudication and/or mutual agreement between the parties thereto."

(2) Plaintiff further requests leave of the Court to file an answer to the intervening petition similar in substance to that filed by the Defendants.

(3) REPUBLIC NATIONAL BANK and Small Business Administration request leave of the Court to amend or interline (a) the tenth line contained in page 4 of its Original Answer to read as follows: "O. K. Super Markets, Inc. so that the Security Agreements and Financing Statements executed by", and (b) add to the last sentence in said paragraph the following: "The balance of said indebtedness being the sum of $252,331.93 plus interest."

13. The following matters will aid in the disposition of the action:

None at this time.

14. The probable length of trial in this case is one-half (½) to one (1) day.

APPROVAL RECOMMENDED:

/s/ Vernon O. Teofan
VERNON O. TEOFAN
Attorney for Plaintiff

/s/ Frank Betancourt
FRANK BETANCOURT
Attorney for Defendant
REPUBLIC NATIONAL BANK OF DALLAS

/s/ Claude Brown
CLAUDE BROWN
Attorney for Defendant
UNITED STATES OF AMERICA

/s/ Lewis A. Jones
LEWIS A. JONES
Attorney for Intervenor
STATE OF TEXAS

/s/ Ted P. MacMaster
TED P. MACMASTER
Attorney for Intervenor
CITY OF DALLAS

APPROVED this 12th day of July, 1973.

/s/ Leo Brewster
United States District Judge

Set for 9:30 a.m., September 17, 1973.

/s/ Leo Brewster
Judge

$ 27,000.00 FORT WORTH, TEXAS April 17, 19 68

For value received, I, we, or either of us, jointly or severally, promise to pay to Kimbell Milling Company d/b/a Kimbell Grocery Company or order, the sum of Twenty Seven Thousand & No/100 ---------- DOLLARS with interest at the rate of 6½ per cent per annum, from Date, interest payable Monthly as it accrues, with both principal and interest payable at Fort Worth, Texas. All past due interest and principal shall bear interest from maturity at the rate of ten per cent per annum.

Payable on demand and if no demand be made, payable as follows:

Payable in monthly installments of $1,000.00 principal, plus interest, beginning May 17, 1968 and a like amount of principal, plus interest, on the 17th of each succeeding month until paid in full both as to principal and interest. The consideration for this note being an advance in goods, wares and merchandise to be delivered between the dates of April 17, 1968 and May 15, 1968.

It is further agreed that if this note is placed in the hands of an attorney for collection or for the purpose of securing same, or if suit is brought thereon, or if same is collected through probate or Bankruptcy proceedings, the makers hereof will pay, in addition to the full amount due, a reasonable attorney's fee. (It is understood and agreed that failure to pay this note or any installment as above promised or any interest thereon when due, shall, at the election of the holder of said note, mature said note, and it shall at once come due and payable.) The sureties, endorsers and guarantors of this note, severally waive extension of time of payment, presentment and demand for payment, (and) protest and notice of protest for the non-payment of this note.

1903 So. Ervay

Dallas, Texas

O. K. Supermarkets, Inc.

By: Harold F. Kimbell
Vice - President

Form No. KG-7022

#.2924

PLAINTIFF'S EXHIBIT 4

BILLS RECEIVABLE

HOUSE FORT WORTH # 306 Page

Name O. K. SUPERMARKETS

Address 1903 So. Ervay, Dallas, Texas Trade Style

Date: April 17, 1968 Maturity Demand/Monthly Int. 6 1/2 %

C/M 2714 D/T Other:

Int. to 2-12-69 $893.10 Paid to

Int. to + $4.35/per day Paid to

Int. to Paid to

Note dated 4/17/68 -- $27,000.00
Payable in monthly installments of $1,000.00 principal, plus interest, beginning May 17, 1968 and a like amount of principal, plus interest, on the 17th of each succeeding month until paid in full both as to principal and interest. The consideration for this note being an advance in goods, wares and merchandise to be delivered between the dates of April 17, 1968 and May 15, 1968. Interest due with first payment -- $146.26 and reduces $5.42 each month thereafter.

APR 19'68JE	27,000.00		27,000.00
MAY 24'68		1,000.00	
MAY 24'68JT		146.26	26,000.00
JUL 3'68		1,000.00	
JUL 8'68JT		140.84	25,000.00
JUL 22'68		1,000.00	
JUL 22'68JT		135.42	24,000.00
FEB 17'69		24,000.00	
FEB 17'69JT		893.10	.00

PLAINTIFF'S EXHIBIT "5"

Memo from

M. D. KIDWELL

OK. Super Mkt
Dallas, Texas

Dan Davis
Republic Nat'l Bank
Dallas, Tex
214-RI7-5538

7 year loan for $300,000.00

Has ask us to
guaranty our pro rata
share of the loan - app. 15%

INTER COMPANY AND OFFICE CORRESPONDENCE

DATE November 19, 1968

TO Mr. W. E. Hartmann AT building

FROM M. D. Kidwell AT building

RE: O K Super Markets, Inc.
Dallas, Texas

Dear Bill:

As you know, these people have been in a bind recently due to the fact that they lost approximately $100,000.00 during the boycott.

Application was made recently to the Small Business Administration for a seven-year loan in the amount of $300,000.00 with the Republic National Bank of Dallas participating. It was our understanding that the Republic National Bank would furnish the money and the SBA would guarantee 90% of the loan. We have now been contacted by Mr. Dan Davis of the Republic National Bank asking us, along with the two other major creditors, to guarantee our pro rata share of the loan, or approximately 15%, based on the amount of money that these people owe us at the present time.

We can see no advantage to our agreeing to guarantee this amount. We, of course, would receive payment of our account in full but we would have to release all of our security and we would have a contingent liability of 15% of the principal balance of this loan and for a period of seven years.

We will appreciate your thinking and your advice in the matter.

Yours truly,

M. D. Kidwell/bt
Credit Department

11/19

What else is there for us to do

Bill Jackson
Caldwell [illegible] $60M
Ted Wilkes $40M
Ted Reynolds

Plaintiff Kimbell's Exhibit 19

DATE November 26, 1968

TO Mr. W. E. Hartmann AT building

FROM M. D. Kidwell AT building

RE: O K Super Markets
Dallas, Texas

I have been trying to reach Mr. Harold Kindle for several days to make an appointment to talk with him and advise him that we could not guarantee his loan as requested. Mr. Kindle called me this morning and advised that their loan for $300,00000 has been approved. I asked Mr. Kindle what happened in regard to the bank's and the SBA's request for the guaranties. Mr. Kindle stated that their attorney and Mr. Earl Cabell went to see the officers of the bank and of the SBA and simply told them that this was ridiculous and if the creditors were willing to guarantee this amount of money they would not need the assistance of the bank or the SBA. Mr. Kindle said, apparently, the bank and the SBA simply dropped the matter of the guaranty and approved their loan without it. Mr. Kindle thinks that they will receive their money sometime next week.

Yours truly,

MDK

M. D. Kidwell/bt
Credit Department

Plaintiff Kimbell's
Exhibit 20

INTER COMPANY AND OFFICE CORRESPONDENCE

DATE January 16, 1969

TO Mr. W. E. Hartmann AT building

FROM M. D. Kidwell AT building

RE: O K Super Markets
Dallas, Texas

You will recall, recently these people told us that the SBA loan had been approved and they had decided to drop the matter of the Personal Guaranties. Now they tell us that it was true that the SBA had agreed to drop the matter of the Guaranty but the Republic National Bank did not.

Attached you will find a Personal Guaranty form which these people and the bank have requested that we sign and covering 4% of the outstanding balance of the loan. Our original liability, of course, will be $12,000.00 and then this amount will reduce accordingly as the principal balance reduces. These people are also asking Cabell Dairies and United Wholesale to execute the same form which will mean that we and the other two creditors will guarantee 12% of the loan.

At the present time this account owes us a principal Note balance of $24,000.00, interest in the amount of $780.00 and $13,000.00 past due on open account. Mr. Harold Kindle has requested that we allow him to pay the principal balance of the Note and the interest immediately upon receipt of the loan and then pay the open account balance in the amount of $13,000.00 at the rate of $200.00 per week and current purchases weekly.

The terms of this loan are six years at $6,000.00 per month including interest. By obtaining this loan the O K Super Markets can pay us in full but we will have a contingent liability for a period of six years. Please advise as to your wishes.

Yours truly,

M. D. Kidwell/bh
Credit Department

Attachment

1-17-69

Mr. Hartmann said "No" b/c Can not get in to a new field & Contingent liabilities also, We want our account paid in full before we release our security.

KCC-A011

Plaintiff Kimbell's Exhibit 21

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SBLG-ME-752,344-00-04-Da

SBA LOAN NO.

GUARANTY
(Loan Guaranty Plan)

✓ , 19—

In order to induce Republic National Bank of Dallas (Bank) to make a loan or loans, or renewal or extension thereof, to O. K. SUPERMARKETS, INC. (Debtor), the undersigned hereby unconditionally guarantees to Bank, its successors and assigns and to the Small Business Administration (SBA) as its interests may appear, the due and punctual payment when due, whether by acceleration or otherwise, in accordance with the terms thereof, of the principal of and interest on and all other sums payable, or stated to be payable, with respect to the note of the Debtor, made by the Debtor to Bank, dated ✓, in the principal amount of $ 300,000.00, with interest at the rate of 8% percent per annum. Such note, and the interest thereon and all other sums payable with respect thereto are hereinafter collectively called "Liabilities." As security for the performance of this guaranty the undersigned hereby mortgages, pledges, assigns, transfers and delivers to Bank certain collateral (if any), listed in the schedule on the reverse side hereof. The term "collateral" as used herein shall mean any funds, guaranties, agreements or other property or rights or interests of any nature whatsoever, or the proceeds thereof, which may have been, are, or hereafter may be, mortgaged, pledged, assigned, transferred or delivered directly or indirectly by or on behalf of the Debtor or the undersigned or any other party to Bank or to the holder of the aforesaid note of the Debtor, or which may have been, are, or hereafter may be held by any party as trustee or otherwise, as security, whether immediate or underlying, for the performance of this guaranty or the payment of the Liabilities or any of them or any security therefor.

The undersigned waives any notice of the incurring by the Debtor at any time of any of the Liabilities, and waives any and all presentment, demand, protest or notice of dishonor, nonpayment, or other default with respect to any of the Liabilities and any obligation of any party at any time comprised in the collateral. The undersigned hereby grants to Bank full power, in its uncontrolled discretion and without notice to the undersigned, but subject to the provisions of any agreement between the Debtor or any other party and Bank at the time in force, to deal in any manner with the Liabilities and the collateral, including, but without limiting the generality of the foregoing, the following powers:

(a) To modify or otherwise change any terms of all or any part of the Liabilities or the rate of interest thereon (but not to increase the principal amount of the note of the Debtor to Bank) to grant any extension or renewal thereof and any other indulgence with respect thereto, and to effect any release, compromise or settlement with respect thereto,

(b) To enter into any agreement of forbearance with respect to all or any part of the Liabilities, or with respect to all or any part of the collateral, and to change the terms of any such agreement;

(c) To forbear from calling for additional collateral to secure any of the Liabilities or to secure any obligation comprised in the collateral;

(d) To consent to the substitution, exchange, or release of all or any part of the collateral, whether or not the collateral, if any, received by Bank upon any such substitution, exchange, or release shall be of the same or of a different character or value than the collateral surrendered by Bank;

(e) In the event of the nonpayment when due, whether by acceleration or otherwise, of any of the Liabilities, or in the event of default in the performance of any obligation comprised in the collateral, to realize on the collateral or any part thereof, as a whole or in such parcels or subdivided interests as Bank may elect, at any public or private sale or sales, for cash or on credit or for future delivery, without demand, advertisement or notice of the time or place of sale or any adjournment thereof (the undersigned hereby waiving any such demand, advertisement and notice to the extent permitted by law), or by foreclosure or otherwise, or to forbear from realizing thereon, all as Bank in its uncontrolled discretion may deem proper, and to purchase all or any part of the collateral for its own account at any such sale or foreclosure, such powers to be exercised only to the extent permitted by law.

The obligations of the undersigned hereunder shall not be released, discharged or in any way affected, nor shall the undersigned have any rights or recourse against Bank, by reason of any action Bank may take or omit to take under the foregoing powers.

In case the Debtor shall fail to pay all or any part of the Liabilities when due, whether by acceleration or otherwise, according to the terms of said note, the undersigned, immediately upon the written demand of Bank, will pay to Bank the amount due and unpaid by the Debtor as aforesaid, in like manner as if such amount constituted the direct and primary obligation of the undersigned. Bank shall not be required, prior to any such demand on, or payment by, the undersigned, to make any demand upon or pursue or exhaust any of its rights or remedies against the Debtor or others with respect to the payment of any of the Liabilities, or to pursue or exhaust any of its rights or remedies with respect to any part of the collateral. The undersigned shall have no right of subrogation whatsoever with respect to the Liabilities or the collateral unless and until Bank or SBA shall have received full payment of all the Liabilities.

The obligations of the undersigned hereunder, and the rights of Bank in the collateral, shall not be released, discharged or in any way affected, nor shall the undersigned have any rights against Bank by reason of the fact that any of the collateral may be in default at the time of acceptance thereof by Bank or later; nor by reason of the fact that a valid lien in any of the collateral may not be conveyed to, or created in favor of, Bank; nor by reason of the fact that any of the collateral may be subject to equities or defenses or claims in favor of others or may be invalid or defective in any way; nor by reason of the fact that any of the Liabilities may be invalid for any reason whatsoever; nor by reason of the fact that the value of any of the collateral, or the financial condition of the Debtor or of any obligor under or guarantor of any of the collateral, may not have been correctly estimated or may have changed or may hereafter change; nor by reason of any deterioration, waste, or loss by fire, theft, or otherwise of any of the collateral unless such deterioration, waste, or loss be caused by the willful act or willful failure to act of Bank.

The undersigned agrees to furnish Bank, or the holder of the aforesaid note of the Debtor, upon demand, but not more often than semiannually, so long as any part of the indebtedness under such note remains unpaid, a financial statement setting forth, in reasonable detail, the assets, liabilities, and net worth of the undersigned.

The undersigned acknowledges and understands that SBA has entered into, or will enter into, a Guaranty Agreement with Bank guaranteeing a portion of Debtor's Liabilities. The undersigned agrees that it is not a coguarantor with SBA and shall have no right of contribution against SBA. The undersigned further agrees that all liability hereunder shall continue notwithstanding payment by SBA under its Guaranty Agreement to Bank.

The term "undersigned" as used in this agreement shall mean the signer or signers of this agreement, and such signers, if more than one, shall be jointly and severally liable hereunder. The undersigned further agrees that all liability hereunder shall continue notwithstanding the incapacity, lack of authority, death, or disability of any one or more of the undersigned, and that any failure by Bank or its assigns to file or enforce a claim against the estate of any of the undersigned shall not operate to release any other of the undersigned from liability hereunder. The failure of any other person to sign this guaranty shall not release or affect the liability of any signer hereof.

It is further agreed and understood that this Guaranty is limited to 4% of the outstanding balance of the loan.

KIMBLE GROCERY COMPANY

ATTEST:

✓
Secretary

By ✓
President

NOTE.--Corporate guarantors must execute guaranty in corporate name, by duly authorized officer, and seal must be affixed and duly attested; partnership guarantors must execute guaranty in firm name, together with signature of a general partner. Formally executed guaranty is to be delivered at the time of disbursement of loan.

LIST ON REVERSE SIDE COLLATERAL SECURING THE GUARANTY

GPO 672-643

SBA Form 148 B (2-64)

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Memo from

M. D. KIDWELL

O.K. Super Markets
Dallas, Texas

Note	# 24,000.00
Interest on note	823.50
Open account -	
Current	10,622.75
Past due	13,000.00
Total owing	48,446.25
Will pay	30,000.00
when loan is received	18,446.25
Less current bal	10,622 75
	7,823 50

Remaining old balance will be paid in not more than 4 weeks and current purchases weekly.

SECURITY AGREEMENT — General

DATE February 12, 1969

A. PARTIES

REPUBLIC NATIONAL BANK OF DALLAS (BANK)
PACIFIC AND ERVAY STREETS, DALLAS, TEXAS
(INFORMATION CONCERNING THIS SECURITY INTEREST MAY BE OBTAINED AT THE OFFICE OF THE BANK SHOWN ABOVE.)

DEBTOR

O. K. SUPER MARKETS, INC.

ADDRESS (RESIDENCE - SHOW COUNTY, IF MAILING ADDRESS DIFFERENT, INSERT MAILING ADDRESS AS WELL.)

1403
~~1407~~ South Ervay Dallas, Texas 75215

B. AGREEMENT

Subject to the applicable terms of this security agreement, debtor grants to bank a security interest in the collateral to secure the payment of the obligation.

C. OBLIGATION

1. The following is the obligation secured by this agreement:
   a. All indebtedness, obligations, and liabilities of any kind of debtor to bank, now or hereafter existing, arising directly between debtor and bank or acquired outright, conditionally, or as collateral security from another by the bank, absolute or contingent, joint or several, secured or unsecured, due or not due, contractual or tortious, liquidated or unliquidated, arising by operation of law or otherwise, direct or indirect, and including, but not as a limitation upon any of the foregoing, any indebtedness, obligation, or liability to bank by debtor as a member of any partnership, syndicate, association or other group, whether incurred by the debtor as principal, surety, indorser, accommodation party or otherwise.
   b. All indebtedness, obligations, and liabilities of debtor to any person to the extent of any participation or interest therein created or acquired for such person, or granted to such person, by bank.
   c. All costs incurred by bank to obtain, preserve, and enforce this security interest, collect the obligation, and maintain and preserve the collateral, and including (but not limited to) taxes, assessments, insurance premiums, repairs, reasonable attorney's fees and legal expenses, feed, rent, storage costs, and expenses of sale.
   d. Interest on the above amounts, as agreed between bank and debtor, or if no such agreement, at the maximum rate permitted by law.
   e. All indebtedness, obligations, and liabilities of O. K. SUPER MARKETS, INC. to bank of the kinds described in this Item C, now existing or hereafter arising.

D. COLLATERAL

1. The security interest is granted in the following collateral:
   a. Describe collateral. Include the following information:
      (1) For oil, gas or other minerals to be extracted, timber to be cut, and fixtures (goods to be affixed to real estate), describe real estate concerned and record owner of the land.
      (2) If debtor's residence is outside the state: give location of consumer goods.

All the debtor's machinery, fixtures, equipment and inventory, now existing or hereafter acquired, all replacements and substitutes therefor, all accessions, attachments and additions thereto, and all tools, parts and equipment now or hereafter added to or used in connection with such machinery and equipment, and all similar property hereafter acquired by debtor. Debtor not authorized to dispose of machinery and equipment. Collateral located at: 1403 S. Ervay, 4123 Oakland, 4630 Hatcher, 3805-7 E. Kiest Blvd, 3026 Grand Ave, 4121 Colonial, R-912 S. Corinth St, 2900 S. Lamar, 1903-19 S. Ervay, 5109 Bexar, 3227 Pennsylvania

   b. All proceeds of, substitutes and replacements for, accessions, attachments, and other additions to, and tools, parts, and equipment used in connection with, the above property. However, such shall not be construed to mean that bank consents to any sale of such collateral.
   c. All property similar to the above hereafter acquired by debtor.
   d. The balance of every deposit account of debtor with bank and any other claim of the debtor against bank, now or hereafter existing and all money, instruments, securities, documents, chattel paper, credits, claims, demands and any other property rights and interests of debtor which at any time shall come into the possession or custody or under the control of the bank or any of its agents, associates or correspondents, for any purpose, and shall include the proceeds of any thereof. The bank shall be deemed to have possession of any of the collateral in transit to or set apart for it or any of its agents, associates or correspondents.
2. Classify goods under one or more of the following Uniform Commercial Code categories:
   - ☐ Consumer goods
   - ☐ Equipment for business use
   - ☐ Inventory
3. ☐ If this block is checked, this is a purchase money security interest, and debtor will use funds advanced to purchase the collateral, or bank may disburse funds direct to the seller of the collateral, and to purchase insurance on the collateral.
4. If any of the collateral is accounts or contract rights, give the location of the office where the records concerning them are kept, if other than debtor's address in Item A: _____

ADDITIONAL TERMS ON BACK.

REPUBLIC NATIONAL BANK OF DALLAS

BY _____ SIGNATURE

_____ TYPED NAME AND TITLE

DEBTOR O K Super Markets Inc

BY _____ SIGNATURE
President

_____ TYPED NAME AND TITLE

BANK MUST SIGN IF THIS SECURITY AGREEMENT IS TO BE FILED AS A FINANCING STATEMENT

Transferred and assigned to Small Business Administration, an agency and instrumentality of the United States Government, without recourse.

Republic National Bank of Dallas

12-30-70
Date

_____ AVP
Name and Title

DEFENDANT'S EXHIBIT

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E. DEBTOR'S WARRANTIES

Debtor warrants as follows:

1. **Financing Statements.** No financing statement covering the collateral or any proceeds thereof is on file in any public office, other than financing statements relating to this security interest.
2. **Ownership Free Of Encumbrances.** Except for the security interest granted hereby, debtor now owns, or will use the proceeds of any advances by bank to become the owner of, the collateral free from any prior lien, security interest or encumbrance.
3. **Fixtures and Accessions.** None of the collateral is affixed to real estate or is an accession to other goods, or will become a fixture or accession, except as expressly set out herein.
4. **Claims of Debtors on Collateral.** Debtor warrants that all account debtors and obligors whose obligations are part of the collateral are to the extent permitted by law prevented from asserting against bank any claims or defenses they have against sellers.
5. **Accuracy of Financial Statements.** All balance sheets, earnings statements and other financial data which have been or may hereafter be furnished to bank to induce it to enter into this agreement or in connection herewith, do or shall truly represent the financial condition and operations of debtor as of the dates and for the periods shown thereon and all other information, reports, papers and data furnished to bank are or shall be, at the time furnished, accurate and correct in all material respects and complete in so far as necessary to give bank a true and accurate knowledge of the subject matter.

F. DEBTOR'S COVENANTS

Debtor covenants as follows:

1. **Ownership of Collateral.** At the time debtor pledges, sells, assigns, or transfers to bank, or grants bank a security interest in any collateral or any interest therein, debtor shall be the absolute owner thereof and shall have the right to pledge, sell, assign or transfer the same. Debtor shall defend the collateral against all claims and demands of all persons at any time claiming the same or any interest therein adverse to bank.
2. **Insurance.** Upon bank's request, debtor shall insure the collateral with companies acceptable to bank against such casualties and in such amounts as bank shall require. All insurance policies shall be written for the benefit of debtor and bank as their interests may appear and such policies or certificates evidencing the same shall be furnished to bank. All policies of insurance shall provide for written notice to bank at least 10 days prior to cancellation. Risk of loss or damage is on debtor to the extent of any deficiency in any effective insurance coverage. Bank is hereby appointed debtor's attorney in fact to endorse any draft or check which may be payable to debtor in order to collect any return or unearned premiums or the proceeds of such insurance.
3. **Maintenance.** Debtor shall keep the collateral in good condition, and free from liens and other security interests, except liens for current taxes not due, and shall not create or suffer to exist any lien or security interest on collateral hereafter acquired except for the security interest hereby granted. Debtor shall pay all costs necessary to obtain, preserve, defend, and enforce this security interest, collect the obligation, and preserve, defend, enforce, and collect the collateral, including, but not as a limitation upon any of the foregoing, the payment of taxes, assessments, insurance premiums, repairs, reasonable attorney's fees and legal expenses, feed, rent, storage costs, and expenses of sales. Whether collateral is or is not in bank's possession, and without any obligation to do so, bank may, at its option, pay any such costs and expenses, discharge encumbrances on collateral, and pay for insurance of collateral. Debtor agrees to reimburse the bank on demand for any payments so made and until such reimbursement, the amount of any such payment, shall be a part of the obligation secured under Item C(1)(c) hereof.
4. **Information and Inspection.** Debtor shall furnish bank with any financial statements or reports, and any information with respect to collateral requested by bank, will allow bank to inspect the collateral, at any time and wherever located, and will allow bank to inspect and copy, or will furnish bank with copies of, all records relating to the collateral and obligation. Debtor shall furnish bank such information as bank may request to identify inventory, accounts receivable, and contract rights assigned hereunder, at the times and in the form and substance requested by bank. Debtor will also, upon request, deliver to bank shipping and delivery receipts evidencing the shipment of goods and invoices evidencing the receipt of, and the payment for, all inventories assigned hereunder.
5. **Additional Documents.** Debtor shall sign any papers furnished by bank which are necessary in the judgment of bank to obtain, maintain and perfect the security interest and to assist bank in complying with the Federal Assignment of Claims Act, where necessary to enable bank to become an assignee under such Act, and any expense of bank so incurred shall be a part of the obligation under Item C(1)(c) hereof.
6. **Parties Liable on Collateral.** Debtor will take necessary steps to preserve the liability of account debtors, obligors, and secondary parties to the obligations which are part of the collateral. Bank shall have no duty to preserve such liability but it may do so, and any expense of bank so incurred shall be a part of the obligation secured under Item C(1)(c) hereof.
7. **Modification of Accounts or Contract Rights.** Debtor will not agree to any material modification of any of the terms of any accounts receivable, contract rights or instruments assigned hereunder without the written consent of bank. Debtor will not, without the written consent of bank, sell, encumber, or otherwise dispose of inventory assigned hereunder except in the ordinary course of business.
8. **Right of Bank to Notify Account and Contract Debtors.** Bank shall have the right at any time, whether debtor is or is not in default, to notify persons obligated on any instruments, accounts, or contracts which are part of the collateral to make payment thereof directly to bank and bank may take control of all proceeds of any of the collateral. Until such time as bank elects to exercise such rights, debtor, as the agent of bank, shall collect and enforce all such contracts and accounts. The cost of such collection and enforcement, including attorney's fees and expenses, shall be borne by debtor, whether the same is incurred by bank or debtor, if paid by bank, such payment shall become a part of the obligation secured under Item C(1)(c) hereof.
9. **Delivery of Receipts to Bank — Rejected Goods.** Upon Bank's demand, debtor will, upon receipt of checks, drafts, cash or other remittances in payment of an instrument, or on account of debtor's accounts or contract rights or received as proceeds of inventory assigned hereunder, deposit all of the same in a special bank account maintained with the bank to be designated by bank over which bank alone has power of withdrawal. The funds in said account shall be held by bank as security for the obligation. Said proceeds shall be deposited in the form received, except for the indorsement of debtor where necessary to permit collection of items, which indorsement debtor agrees to make, but which the bank is authorized to make on debtor's behalf. Pending such deposits debtor agrees that it will not mingle any such checks, drafts, cash or other remittances with any of debtor's funds or property, but will hold them separate and apart therefrom and upon an express trust for bank until deposit thereof is made in the special account. Bank will, from time to time, apply the whole or any part of the collected funds on deposit in the special account against the principal or interest of any loans made hereunder, or debtor's other indebtedness secured hereby. Any portion of said funds on deposit which bank elects not to so apply may be paid by bank to debtor.

Unless bank notifies debtor in writing that it dispenses with any one or more of the following requirements, debtor will:

a. inform bank immediately of the rejection of goods, delay in delivery or performance, or claims made, in regard to any account or contract right assigned to bank;

b. keep returned goods segregated from debtor's other property, and hold such goods as trustee for bank until it has paid the bank the amount loaned against the related account, and deliver such goods on demand to bank, which shall have a security interest in such goods;

c. pay bank the unpaid portion of any assigned account or contract right (1) if such account is is not paid promptly after its maturity; (2) if purchaser does not accept the goods or services; (3) if bank shall at any time reject the account as unsatisfactory; and until such payment is made by debtor, bank may retain any such account or contract rights as security and may charge any deposit account of debtor with any such amounts.

10. **Books of Account.** Debtor will, at all times, maintain accurate books and records covering the collateral. Immediately upon the execution of this agreement, debtor will mark all books and records with an entry showing the absolute assignment of all accounts and contracts assigned hereunder to bank, and bank is hereby given the right to audit the books and records of debtor relating to said collateral at any time, and from time to time, as bank deems proper.
11. **Disposition of Inventory.** At any time the disposition of inventory assigned hereunder gives rise to an account, debtor shall immediately notify bank of the disposition of said inventory, or part thereof, and assign said account to bank. Each such account, and any other account submitted to bank hereunder, will represent the valid and legally enforceable indebtedness of a bona fide customer arising from the sale or lease of goods or rendition of services by debtor, will not be subject to return for credit or substitution for any reason known to debtor, and will be subject to no set-offs, counter-claims, adjustments, or defenses; such goods will have been delivered to the customer and such services will have been performed for the customer, and such goods and services will have been accepted by the customer. The amount shown as to each account on debtor's books and on the assignment schedule, if any, will be the true and undisputed amount owing and unpaid thereon.
12. **Contract Rights Arising From Disposition of Inventory.** At any time the disposition of inventory assigned hereunder gives rise to a contract right, debtor shall immediately notify bank of the disposition of said inventory, or part thereof, and assign said contract right to bank. Said contract rights, and any other contract rights submitted to bank hereunder, shall be evidenced by existing, binding written contracts between debtor and third party, shall not be evidenced by any instrument or chattel paper, no set-offs or counter-claims thereto shall exist, no agreement shall have been made for any modification, deduction or discount, and no partial payment shall have been made except as revealed to bank in writing.
13. **Location of Accounts Receivable, Contracts and Inventory.** Debtor shall give bank written notice of each office of debtor in which records of debtor pertaining to accounts and contracts which are collateral are kept, and each location at which inventory which is collateral is or will be kept, and of any change of said office, offices, location, or locations. Except as such notice is given, all records of debtor pertaining to accounts and contracts are and shall be kept in the location shown at the beginning hereof, and all inventory is and shall be kept at debtor's address shown at the beginning hereof.
14. **Notice of Changes.** Debtor will notify bank of any change occurring in or to the collateral, of a change in debtor's residence, or in any fact or circumstance warranted or represented by debtor in this agreement or furnished to bank or of any event of default occurs, prior to or immediately following the occurrence thereof.
15. **Use and Removal of Collateral.** Debtor will not use the collateral illegally or encumber the same and will not permit the collateral to be affixed to real or personal property without the prior written consent of bank. Debtor will not permit any of the collateral to be removed from the locations specified herein without the written consent of the bank. Debtor will not sell, lease, otherwise transfer, manufacture, process or assemble the collateral, or furnish the same under contracts of service, except goods identified herein as inventory.
16. **Possession of Collateral.** Debtor will transfer possession of all instruments, securities, documents, and chattel paper which are part of the collateral to the bank immediately, or, if hereafter acquired, immediately following acquisition, appropriately indorsed to bank's order, or with appropriate powers, and, regardless of the form of such indorsement, debtor hereby waives presentment, demand, notice of dishonor, protest, and notice of protest, and all other notices with respect thereto.
17. **Chattel Paper.** Debtor has or will perfect a security interest, using a method satisfactory to the bank, in goods covered by chattel paper which is part of the collateral.

G. RIGHTS AND POWERS OF BANK

1. Bank may, in its discretion, before or after default: require debtor to give possession or control of the collateral to bank; indorse as debtor's agent any instruments, securities, or chattel paper in the collateral; contact account debtors directly to verify information furnished by debtor; take control of proceeds, including stock received as dividends or by reason of stock splits, and use cash proceeds to reduce any part of the obligation; take any action debtor is required to take or any other necessary action to obtain, preserve, and enforce this security interest, and maintain and preserve the collateral, without notice to debtor, and add costs of same to the obligation (but bank is under no duty to take any such action); release collateral in its possession to debtor, temporarily or otherwise; require additional collateral; reject as unsatisfactory any property hereafter offered by debtor as collateral; set standards, from time to time to govern what may be used as after acquired collateral; designate, from time to time, a certain per cent of the collateral as the loan value and require debtor to maintain the obligation at or below such figure; take control of funds generated by the collateral, such as cash dividends, interest, and proceeds or refunds from insurance, and use same to reduce any part of the obligation; vote any stock which is part of the collateral; and exercise all other rights which an owner of such stock may exercise. Bank may at any time in its discretion transfer any of the collateral or evidence thereof into its own name or that of its nominee and receive the proceeds therefrom and hold the same as security for the obligation, or apply the same thereon. Bank may, but shall be under no duty to, demand, collect, receipt for, settle, compromise, adjust, sue for, foreclose, or realize upon collateral, in its own name or in the name of debtor, as the bank may determine. Bank shall not be liable for the failure to collect any account or enforce any contract right or for any act or omission on the part of the bank, its officers, agents, or employees, except willful misconduct. The foregoing rights and powers of bank shall be in addition to, and not a limitation upon, any rights and powers of bank given by law, custom, elsewhere by this agreement, or otherwise.

H. DEFAULT

1. **Events of Default.** Debtor shall be in default under this agreement upon the happening of any of the following events or conditions:
   a. Default in the timely payment or performance of any obligation, covenant or liability contained herein or secured hereby;
   b. Any warranty, representation or statement made or furnished to bank by or in behalf of debtor proves to have been false in any material respect when made or furnished;
   c. Any event which results in the acceleration of the maturity of the indebtedness of debtor to others under any indenture, agreement or undertaking;
   d. Substantial change in any fact warranted or represented in this agreement;
   e. Sale, loss, theft, destruction, encumbrance, or transfer of any collateral, or substantial damage thereto;
   f. Any time the bank believes that the prospect of payment of any obligation secured hereby or performance of this agreement is impaired;
   g. On debtor's death, incapacity, dissolution, merger or consolidation, termination of existence, insolvency, business failure, appointment of a receiver for any part of the collateral, commission of an act of bankruptcy, assignment for the benefit of creditors or the commencement of any proceeding under any bankruptcy or insolvency law by or against debtor, or any partnership of which debtor is a partner, or any maker, drawer, acceptor, indorser, guarantor, surety, accommodation party, or other person liable upon or for any obligation or collateral;
   h. Modification of any contract, the rights to which are part of the collateral;
   i. Levy on, seizure, or attachment of the collateral, or any part thereof;
   j. Judgment against debtor;
   k. Filing any financing statement with regard to the collateral, other than relating to this security interest; or attachment of any lien except a lien for current ad valorem taxes not yet due to any portion of the collateral;
   l. Bank receives notice of a purchase money security interest in inventory covered by this agreement;
   m. Failure of debtor immediately to furnish additional collateral satisfactory to bank upon the request of bank.
2. **Remedies of Bank upon Default.** When an event of default occurs, and at any time thereafter, bank may declare all obligations secured hereby immediately due and payable and may proceed to enforce payment of the same and to exercise any and all of the rights and remedies provided by the Uniform Commercial Code as well as all other rights and remedies possessed by bank under this agreement or otherwise. Bank may require debtor to assemble the collateral and make it available to bank at any place to be designated by the bank which is reasonably convenient to both parties. Unless the collateral is perishable or threatens to decline speedily in value or is of a type customarily sold on a recognized market, bank will give debtor reasonable notice of the time and place of any public sale thereof or of the time after which any private sale or any other intended disposition thereof is to be made. Expenses of retaking, holding, preparing for sale, selling, leasing, or the like shall include bank's reasonable attorney's fees and legal expenses. Bank shall be entitled to immediate possession of all books and records evidencing any accounts and contract rights covered by this agreement and shall have authority to enter upon any premises upon which the same may be situated and remove the same therefrom. Debtor shall be entitled to any surplus and shall be liable to bank for any deficiency arising from accounts, contract rights or chattel paper included in the collateral through sale thereof to bank. If bank disposes of the collateral following default, the proceeds of such disposition available to satisfy the obligation shall be applied by bank to the obligation in such order and in such manner as bank in its discretion shall decide.

I. GENERAL

1. **Assignment of Collateral by Bank.** The bank may assign all or any part of the obligation, and may assign, transfer, or deliver to any transferee of any of the obligation any or all of the collateral, and thereafter shall be fully discharged from all responsibility with respect to the collateral so assigned, transferred or delivered. Such transferee shall be vested with all the powers and rights of the bank hereunder with respect to such collateral, but the bank shall retain all rights and powers hereby given with respect to any of the collateral not so assigned or transferred.
2. **Waiver.** No delay on the part of the bank in exercising any power or right shall operate as a waiver thereof; nor shall any single or partial exercise of any power or right preclude other or further exercise thereof or the exercise of any other power or right. No waiver by bank of any right hereunder or of any default by debtor shall be binding upon bank unless in writing, and no failure by bank to exercise any right hereunder or waiver of any default of debtor shall operate as a waiver of any other or further exercise of such right or of any further default.
3. **Parties Bound.** The rights of bank hereunder shall inure to the benefit of its successors and assigns. The terms of this agreement shall be binding upon the heirs, executors, administrators, successors, and assigns of the parties hereto. All representations, warranties and agreements of debtor are joint and several if debtor is more than one and shall bind debtor's personal representatives, heirs, successors and assigns. This agreement shall constitute a continuing agreement, applying to all future as well as existing transactions, whether or not of the character contemplated at the date of this agreement, and if all transactions between the bank and the debtor shall be at any time closed, shall be equally applicable to any new transactions thereafter, and shall so continue in force notwithstanding any change in any partnership party hereto, whether such change occurs through death, retirement or otherwise.
4. **Definitions.** Unless the context indicates otherwise, definitions in the Uniform Commercial Code apply to words and phrases in this agreement; if Code definitions conflict, Article 9 definitions apply.
5. **Notice.** Notice mailed postage prepaid to debtor's address given above or to debtor's most recent address as shown by notice of change on file with bank at least 5 days prior to the related action (or if the Uniform Commercial Code elsewhere specifies a longer period, such longer period) shall be deemed reasonable.
6. **Modifications.** No provision hereof shall be modified or limited except by a written agreement expressly referring hereto and to the provision so modified or limited and signed by both parties to this agreement, nor by course of conduct, usage of trade, or by the law merchant.
7. **Severability.** The unenforceability of any provision of this agreement shall not affect the enforceability or validity of any other provision hereof.
8. **Financing Statement.** Bank is authorized on behalf of debtor to complete and sign one or more financing statements with respect to any collateral covered by this agreement and to file the same in any appropriate office or place.
9. **Applicable Law.** This agreement shall be construed according to the laws of the State of Texas.
10. **Venue.** It is agreed that venue in any proceeding hereunder shall be in Dallas County, Texas.

Uniform Commercial Code–FINANCING STATEMENT–Form UCC-1 (Rev. 9-71)

THE ODEE COMPANY, PUBLISHERS, DALLAS, TEXAS 75201

IMPORTANT—Read instructions on back before filling out form

This Financing Statement is presented to a Filing Officer for filing pursuant to the Uniform Commercial Code

3. Maturity Date (if any):

1. Debtor(s) (Last name first) and Mailing Address:

O. K. Super Markets, Inc.
1403 S. Erway
Dallas, Texas 75215

2. Secured Party(ies) Name and Address:

Republic National Bank of Dallas
Pacific and Erway Streets
Dallas, Texas 75202

4. For Filing Officer (Date, Time, Number and Filing Office):

SECRETARY OF STATE
FEB. 18, 69
#254934

5. This Financing Statement covers the following types (or items) of collateral. (WARNING: If collateral is crops or fixtures, read instructions on back.)

6. Name and Address of Assignee of Secured Party: (Use this space to describe collateral, if needed)

All the debtor's machinery, fixtures, equipment and inventory, now existing or hereafter acquired, all replacements and substitutes therefor, all accessions, attachments and additions thereto, and all tools, parts and equipment now or hereafter added to or used in connection with such machinery and equipment, and all similar property hereafter acquired by debtor. Debtor not authorized to dispose of machinery and equipment. Collateral located at: 1403 S. Erway, 4123 Oakland, 4630 Hatcher, 3305-7 E. Kiest Blvd., 3026 Grand Ave., 4121 Colonial, R-912 S. Corinth St., 2900 N. Lamar, 1903-19 S. Erway, 5109 Bexar, 3227 Pennsylvania.

Check ☒ if covered: ☐ Proceeds of collateral are also covered. ☐ Products of collateral are also covered. Number of additional sheets presented_____

7. This Statement is filed without the Debtor's signature to perfect a security interest in collateral

(Please check appropriate box)
- ☐ already subject to a security interest in another jurisdiction when it was brought into this state, or
- ☐ which is proceeds of the original collateral described above in which a security interest was perfected, or
- ☐ already subject to a financing statement filed in another county, or
- ☐ already subject to a pre-code perfected security interest.

O. K. SUPER MARKETS, INC.

By_____
Signature(s) of Debtor(s)

REPUBLIC NATIONAL BANK OF DALLAS

By_____
Signature(s) of Secured Party(ies)

(1) Filing Officer Copy—Numerical

STANDARD FORM – FORM UCC-1 (REV. 9-71) APPROVED BY SECRETARY OF STATE OF TEXAS–THE ODEE COMPANY, DALLAS, TEXAS 75201

SBA Loan No.
SBLG-ME-752,344-00-04-Dal

NOTE

Dallas, Texas 75215
(City and State)

$ 300,000.00 (Date) February 12, 19 69

For value received, the undersigned promises to pay to the order of

Republic National Bank of Dallas

at its banking house in the city of Dallas, State of Texas,

or at Payee's option, at such other place as may be designated from time to time by the Payee, - - - - - - - - - -
(Write out amount)

- - - - - -THREE HUNDRED THOUSAND AND NO/100- dollars,

with interest on unpaid principal computed from the date of each advance to the undersigned at the rate of eight (8) per-cent per annum, payment to be made in installments as follows:

$4,676.00, including principal and interest, payable monthly, beginning one (1) month from date hereof and $4,676.00 on the same date of each succeeding calendar month thereafter until paid in full, provided that all principal and interest not sooner paid shall become due and payable seven (7) years from the date hereof; and each said installment payment, when received, shall be applied by the holder hereof, first to interest accrued to the date of receipt of said payment, and the balance, if any, on account of the principal hereof.

Payment of any installment of principal or interest owing on this Note may be made prior to the maturity date thereof without penalty.

The term "Indebtedness" as used herein shall mean the indebtedness evidenced by this Note, including principal, interest, and expenses, whether contingent, now due or hereafter to become due and whether heretofore or contemporaneously herewith or hereafter contracted. The term "Collateral" as used in this Note shall mean any funds, guaranties, or other property or rights therein of any nature whatsoever or the proceeds thereof which may have been, are, or hereafter may be, hypothecated, directly or indirectly by the undersigned or others, in connection with, or as security for, the Indebtedness or any part thereof. The Collateral, and each part thereof, shall secure the Indebtedness and each part thereof. The covenants and conditions set forth or referred to in any and all instruments of hypothecation constituting the Collateral are hereby incorporated in this Note as covenants and conditions of the undersigned with the same force and effect as though such covenants and conditions were fully set forth herein.

SBA Form 154 (1-65)

Bank

Transferred and assigned to Small Business Administration, an agency and instrumentality of the United States Government, without recourse.

Republic National Bank of Dallas

12-30-70
Date

[illegible], V.P.
Name and Title

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The Indebtedness shall immediately become due and payable, without notice or demand, upon the appointment of a receiver or liquidator, whether voluntary or involuntary, for the undersigned or for any of its property, or upon the filing of a petition by or against the undersigned under the provisions of any State insolvency law or under the provisions of the Bankruptcy Act of 1898, as amended, or upon the making by the undersigned of an assignment for the benefit of its creditors. Payee is authorized to declare all or any part of the Indebtedness immediately due and payable upon the happening of any of the following events: (1) Failure to pay any part of the Indebtedness when due; (2) nonperformance by the undersigned of any agreement with, or any condition imposed by, Payee and Small Business Administration (hereinafter called "SBA"), or either of them, with respect to the Indebtedness; (3) Payee's discovery of the undersigned's failure in any application of the undersigned to Payee or SBA to disclose any fact deemed by Payee to be material or of the making therein or in any of the said agreements, or in any affidavit or other documents submitted in connection with said application or the indebtedness, of any misrepresentation by, on behalf of, or for the benefit of the undersigned; (4) the reorganization (other than a reorganization pursuant to any of the provisions of the Bankruptcy Act of 1898, as amended) or merger or consolidation of the undersigned (or the making of any agreement therefor) without the prior written consent of Payee; (5) the undersigned's failure duly to account, to Payee's satisfaction, at such time or times as Payee may require, for any of the Collateral, or proceeds thereof, coming into the control of the undersigned; or (6) the institution of any suit affecting the undersigned deemed by Payee to affect adversely its interest hereunder in the Collateral or otherwise. Payee's failure to exercise its rights under this paragraph shall not constitute a waiver thereof.

Upon the nonpayment of the Indebtedness, or any part thereof, when due, whether by acceleration or otherwise, Payee is empowered to sell, assign, and deliver the whole or any part of the Collateral at public or private sale, without demand, advertisement or notice of the time or place of sale or of any adjournment thereof, which are hereby expressly waived. After deducting all expenses incidental to or arising from such sale or sales, Payee may apply the residue of the proceeds thereof to the payment of the Indebtedness, as it shall deem proper, returning the excess, if any, to the undersigned. The undersigned hereby waives to the full extent permitted by law all right of redemption or appraisement whether before or after sale. At any such sale payee may become the purchaser of the whole or any part of the Collateral free from any right of redemption so far as permitted by law. Without limiting or affecting such power of sale, Payee is further empowered, upon the nonpayment of the Indebtedness, or any part thereof, when due, to collect or cause to be collected or otherwise to be converted into money all or any part of the Collateral, in the name of Payee or the undersigned or otherwise, by suit or otherwise, and to surrender, compromise, release, renew, extend, exchange, or substitute any item of the Collateral in transactions with the undersigned or any third party, irrespective of any assignment thereof by the undersigned, and without prior notice to or consent of the undersigned or any assignee. Whenever any item of the Collateral shall not be paid when due, or otherwise shall be in default, whether or not the indebtedness, or any part thereof, has become due, Payee shall have the same rights and powers with respect to such item of the Collateral as are granted in respect thereof in this paragraph in case of nonpayment of the Indebtedness, or any part thereof, when due. None of the rights, remedies, privileges, or powers of Payee expressly provided for herein shall be exclusive, but each of them shall be cumulative with and in addition to every other right, remedy, privilege, and power now or hereafter existing in favor of Payee, whether at law or in equity, by statute or otherwise.

The undersigned agrees to take all necessary steps to administer, supervise, preserve, and protect the Collateral; and regardless of any action taken by Payee, there shall be no duty upon Payee in this respect. The undersigned shall pay all expenses of any nature, whether incurred in or out of court, and whether incurred before or after this Note shall become due at its maturity date or otherwise, including but not limited to reasonable attorney's fees and costs, which Payee may deem necessary or proper in connection with the satisfaction of the Indebtedness or the administration, supervision, preservation, protection (including, but not limited to, the maintenance of adequate insurance) of or the realization upon the Collateral. Payee is authorized to pay at any time and from time to time any or all of such expenses, add the amount of such payment to the amount of the Indebtedness, and charge interest thereon at the rate specified herein with respect to the principal amount of this Note.

The security rights of Payee and its assigns hereunder shall not be impaired by Payee's sale, hypothecation or rehypothecation of any note of the undersigned or any item of the Collateral, or by any indulgence, including but not limited to (a) any renewal, extension, or modification which Payee may grant with respect to the Indebtedness or any part thereof, or (b) any surrender, compromise, release, renewal, extension, exchange, or substitution which Payee may grant in respect of the Collateral, or (c) any indulgence granted in respect of any endorser, guarantor, or surety. The purchaser, assignee, transferee, or pledgee of this Note, the Collateral, any guaranty, and any other document (or any of them), sold, assigned, transferred, pledged, or repledged, shall forthwith become vested with and entitled to exercise all the powers and rights given by this Note and all applications of the undersigned to Payee or SBA, as if said purchaser, assignee, transferee, or pledgee were originally named as Payee in this Note and in said application or applications.

ATTEST:

Glen D. Kindle, Secretary

O. K. SUPERMARKETS, INC.

By ~~Harold L. Kindle~~

Harold L. Kindle, President

Note.--Corporate applicants must execute Note, in corporate name, by duly authorized officer, and seal must be affixed and duly attested; partnership applicants must execute Note in firm name, together with signature of a general partner.

NOTE: Return original and 2 executed copies to SBA

SMALL BUSINESS ADMINISTRATION

APPLICATION FOR LOAN UNDER BLANKET GUARANTY

SBA LOAN NO.
SBLG-HS-752,344-00-04-DAL

Regional Director
Small Business Administration

Pursuant to provisions of the Blanket Loan Guaranty Agreement executed between the lender and Small Business Administration, dated November 22, 1968, it is requested that the Loan described below be included under the provisions of the said Agreement and that SBA guarantee said Loan to the extent of 90.0 %.

NAME AND ADDRESS OF APPLICANT: (Include ZIP Code)

O. K. Supermarkets, Inc.
1403 South Ervay
Dallas, Texas 75215

AMOUNT OF LOAN: $ 300,000

MATURITY: 7 years

INTEREST RATE: 8%

TELEPHONE: HA 8 - 6794

PRODUCT OR SERVICE FURNISHED:

Retail Groceries

PROPRIETORSHIP ☐ PARTNERSHIP ☐ CORPORATION ☒

PURPOSES OF LOAN: (List)	AMOUNT:	
Debt payment	$200,000	
Working capital-inventory	30,000	
" " -All other	70,000	
	TOTAL	$ 300,000

Additional information requested on the reverse side hereof is enclosed. Lender believes that there is reasonable assurance of repayment but is unable to make the loan unless SBA authorizes the guaranty requested herein. Lender hereby certifies that, to the best of its knowledge: (a) the applicant's principals are of good character; and (b) the fees of applicant's representatives, if any, as set forth in item 2 of "Applicant's Statement," are reasonable.

REPUBLIC NATIONAL BANK
LENDER

By: [signature]

Date: November 22, 1968

Assistant Vice President
TITLE

SMALL BUSINESS ADMINISTRATION

AUTHORIZATION OF LOAN GUARANTY

Your request for SBA Guaranty of 90 % of the above loan to be made and serviced by you is hereby approved subject to the loan conditions, if any, stated on the reverse side of this form under authority of Section 7(a) of the Small Business Act of 1958, as amended and subject to the terms of the Blanket Loan Guaranty Agreement referred to above.

ADMINISTRATOR

By: R. E. Crain
Regional Director
TITLE
SMALL BUSINESS ADMINISTRATION

Date: January 8, 1969

(Instructions on Reverse)

DEFENDANT'S EXHIBIT "5" & "9"

SBA FORM 751 (9-68) REF: NO 510-1 PREVIOUS EDITIONS ARE OBSOLETE

(OVER)

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ADDITIONAL LOAN CONDITIONS REQUIRED BY SBA

1. Security interest in machinery, equipment and fixtures and security interest in inventory.
2. The personal guaranty of Harold Lee Kindle, Glen D. Kindle, and Joe Elston on SBA Form 148B.
3. Guaranty of 4% of the outstanding balance by each of the following firms: Cabell's Dairies, United Wholesale, and Kimble Grocery and Company.
4. Evidence satisfactory to bank and SBA that the plan as outlined in letter dated December 3, 1968, relative to ownership has been put into execution.
5. As additional security, pledge of all outstanding stock with voting rights.
6. Immediately after disbursement, Bank to furnish SBA the following instruments:
   a. Copy of Note (SBA-154) signed and dated;
   b. Original and first copy of Report of Transactions (SBA-172);
   c. Signed copy of Bank's loan agreement, if one is prepared;
   d. Copy of each Guaranty (SBA-148B) signed and dated; and
   e. Copy of Bank's settlement sheet showing how funds were disbursed, if one is prepared.

INSTRUCTIONS

1. An original and two executed copies of this form are to be submitted to SBA. If the guaranty is approved, an executed copy will be returned showing that the guaranty is in effect.

2. Attach with the application:
   (a) Applicant's Statement, SBA Form 528A and all attachments required by such Form.
   (b) A copy, or summarization, of lender's appraisal of the collateral. SBA will assist in appraisals if requested.
   (c) Pertinent credit information developed on applicant, noting any receivership or bankruptcy action.
   (d) A copy of the loan terms lender intends imposing (e.g., proposed loan agreement or similar document).

GENERAL REQUIREMENTS

1. The first disbursement of the loan must be made not later than six months, and no disbursement shall be made later than 12 months, from the date of SBA's Authorization of Loan Guaranty (see obverse), unless such periods are extended by written consent of SBA.

2. Where loan funds will be used for construction purposes, and the contract or subcontracts are in excess of $10,000, the Applicant must execute and submit with his application "Applicant's Agreement of Compliance," SBA Form 601, which is a non-discrimination agreement issued pursuant to Executive Order 11246.

3. The Government must regulate fees paid by Applicant to its attorney, accountant, or other representative. In this regard, please furnish Applicant SBA Form 394 explaining the policy.

SBA LOAN POLICY

SBA will not extend financial assistance:
(1) If the funds are otherwise available on reasonable terms from normal lending sources or the personal resources of the principals.
(2) If the loan is to (a) pay off a creditor or creditors of the applicant who are inadequately secured and in a position to sustain loss, (not applicable to Economic Opportunity Loans), (b) provide funds for distribution or payment to the principals of the applicant, or (c) replenish funds previously used for such purposes.
(3) If the loan allows speculation in any kind of property.
(4) If the applicant is a nonprofit enterprise.
(5) To a consumer cooperative.
(6) If the loan finances recreational or amusement facilities, unless the facilities contribute to the health or well-being of the general public.
(7) If the applicant is a newspaper, magazine, book publishing company, radio broadcasting company or similar enterprise.
(8) If any of the gross income of the applicant (or of any of its principal owners) is derived from gambling activities.
(9) If the loan provides funds to an enterprise primarily engaged in lending or investments.
(10) If the loan finances real property that is, or is to be, held for sale or investment; or finances an agricultural activity.
(11) If the loan encourages monopoly or is inconsistent with the accepted standards of the American system of free competitive enterprise.
(12) If the loan is used to relocate a business for other than sound business purposes.
(13) Under some circumstances (except for Economic Opportunity Loans) to effect a change in ownership of a business.

NOTE: If you have any questions call or write the SBA Regional Office.

BLANKET LOAN GUARANTY AGREEMENT BETWEEN

AND THE SMALL BUSINESS ADMINISTRATION

An agreement, made the 1st day of November, 1967 by and between

Republic National Bank of Dallas (Lender)

and Small Business Admini-tration, an agency of the United States Government (SBA):

WITNESSETH:

WHEREAS, it is the intention of the parties to establish a mutual arrangement and understanding for the making by Lender and the guaranteeing by SBA of loans to small business concerns in the furtherance of their respective interests and the interest of the small business economy as provided in the Small Business Act of 1958, as amended (SBA Act);

NOW, THEREFORE, in consideration of the mutual promises contained herein, the parties represent and agree, as follows:

1. **Application for Guaranty.** This agreement shall relate only to any new loan which has been approved by Lender and SBA in accordance with their respective credit policies and the conditions of guaranty set forth in the SBA Act and SBA Rules and Regulations. Any loan approved by Lender contingent upon SBA's guaranty may be referred to SBA for authorization upon the separate applications of Lender* and the loan applicant*.

2. **Approval of Guaranty.** SBA shall either authorize the guaranty by returning a copy of the application showing written approval of such authorization, or decline the guaranty by written notice to the Lender. If the application for any guaranty is not approved as submitted by the Lender but can be approved by modifying the written loan conditions in a manner acceptable to both Lender and SBA, the guaranty may be authorized by SBA. Any change thereafter in the authorized loan conditions shall be subject to prior written approval by SBA.

3. **Closing and Disbursement of Loans.** Lender shall close and disburse each loan in accordance with the terms and conditions upon which the loan and guaranty were approved. Lender shall cause to be executed a note* and any additional instruments and take such other actions which shall, consistent with prudent closing practices, be required in order fully to protect or preserve the interests of Lender and SBA in the loan. Immediately after a loan is closed, Lender shall furnish SBA with a copy of the executed note and loan agreement. Upon its request, SBA shall also be entitled to examine copies of other security instruments or loan documents held by Lender which relate to loans made pursuant to this agreement.

4. **Loan Servicing.** Lender or SBA, whichever is the holder of any note, shall not, without the prior written consent of the other party: (a) purchase hazard or liability insurance with respect to any collateral; (b) make or consent to any transfer or assignment of any note or to any alteration in its terms or the terms of security instruments; (c) make or consent to any release, conveyance, substitution or exchange of any collateral having a value, as reasonably determined by the holder, which is more than 10 percent of the outstanding loan balance; (d) accelerate the maturity of the note; (e) sue upon the note, collateral or instrument; or (f) waive any claim against any borrower or guarantor, standby creditor, or other obligor arising out of any note or security instrument. All other servicing actions shall be the responsibility of the holder who shall follow accepted standards of loan servicing employed by prudent lenders generally.

5. **Quarterly Report of Disbursement and Repayment.** By the 10th day of the month following each calendar quarter, Lender shall furnish to SBA a report* showing each such loan on which Lender made disbursement or on which borrower made payment on account of interest and/or principal during the preceding calendar quarter.

6. **Guaranty Charge.** Within 10 days after being billed therefor, Lender shall pay SBA for each calendar quarter, a guaranty fee computed at the rate of one-half percent (½%) per annum (per diem basis) of that part of the guaranteed percentage of unpaid principal balances of disbursed loans guaranteed hereunder. The guaranty fee payable hereunder shall not be added to any amount which a borrower is obligated to pay under a loan.

7. **Notice of Borrower's Default and Demand for Purchase.** In the event any borrower defaults upon the note or any security agreement, or fails to make any payment when due of principal or interest on the note, Lender shall notify SBA of such default in writing within 30 days after the happening or knowledge thereof, unless cured; such notice is a condition precedent to Lender's demand for purchase. In the event Lender desires to accelerate the indebtedness, request for the written consent of SBA may be made a part of that notice. If any borrower shall be in default and such default is not cured within 60 days after the happening thereof, Lender shall have the right to make demand in writing for the purchase by SBA of the guaranteed percentage of the amount then owing on such loan. The 60-day period may be waived if the parties agree that acceleration of the note is necessary at an earlier date.

SBA Form 750 (4-67) Replaces FA 1Form 3 (11-62) Which is Obsolete

8. Purchase by SBA. In making its written demand for SBA to purchase its guaranteed percentage of any loan hereunder, Lender shall thereby certify that the loan has been disbursed and serviced in compliance with this agreement and that the provisions of this agreement remain in full force and effect with respect to said loan. Within 20 days after receipt of Lender's demand, SBA shall pay to Lender the guaranteed percentage of the amount then owing on such loan (including appropriate adjustment for interest and charges) and Lender shall issue to SBA a participation certificate* evidencing SBA's interest. Lender shall hold the note, all the collateral therefore and all instruments in connection therewith; provided however that subsequent to the purchase by SBA of its guaranteed percentage in any such loan and upon written demand by SBA, Lender shall within 5 days after receipt of such demand transfer to SBA, without recourse, the note, collateral, and instruments for said loan and simultaneously therewith SBA shall issue to Lender a certificate of interest* evidencing Lender's interest retained in said loan.

9. Fees or Commissions. Lender shall not directly or indirectly charge or receive any bonus, fee, commission, or expense in any form in connection with the making or servicing of any such loan, except charges or expenses incurred, or for actual services rendered.

10. Sharing of Repayment Proceeds. Any and all repayments, security or guaranty of any nature, including but not limited to rights of setoff and counterclaim, which Lender or SBA jointly or severally, may at any time receive or have in any loan guaranteed hereunder, shall repay and secure the interests of Lender and SBA in the same proportion as such interests bear respectively to the entire unpaid balance of such guaranteed loan. In the event Lender makes any loan or advance to a borrower subsequent to a loan made under this guaranty agreement, Lender shall notify SBA of such loan or advance and, if circumstances require, enter into a written agreement with SBA providing for the application of collateral (or any moneys realized therefrom) to the respective loans in a manner satisfactory to the parties hereto.

11. Payment of Expenses. All reasonable expenses incurred by SBA or Lender which are not recoverable from borrower shall be shared ratably by SBA and Lender in accordance with their respective interests in any such loan.

12. SBA Purchase Privilege. Anytime any loan guaranteed hereunder shall be in default in payment for more than 90 days, SBA may at its option give written notice to the Lender that SBA will purchase its guaranteed percentage, or the loan in its entirety, 10 days after receipt of said notice by the Lender. Upon such purchase date, the transfer of the note and related instruments, without recourse, to SBA and of a certificate of interest to the Lender shall be simultaneously completed.

13. Termination. Either party hereto, by giving not less than 10 days prior written notice by certified mail to the other party, may terminate the provisions of this agreement; such termination shall not apply to any loan previously authorized by SBA hereunder. Lender may at any time prior to purchase by SBA terminate the provisions of this agreement as to any individual loan upon receipt of notice of termination by SBA. The provisions of this agreement shall be terminated in the case of any loan if demand for SBA to purchase is not made within 60 days following the stated maturity date of the note.

IN WITNESS WHEREOF, Lender has caused this agreement to be executed on its behalf by its duly authorized officer or officers and its corporate seal to be hereunto affixed, and Small Business Administration has caused this agreement to be executed on its behalf by its Regional Director, at its Dallas, Texas Office Office, the day and year first above written.

(SEAL)

ATTEST:

William Frank Stevens
TITLE
Assistant Cashier

Republic National Bank of Dallas
LENDER

By Charles H. Porter Jr.
TITLE
Senior Vice President

SMALL BUSINESS ADMINISTRATION

By
TITLE
Regional Director

*Form to be furnished by SBA

SBA Form 750 (4-67)

STATEMENT

O K Super Markets #3
Dallas, Texas
Account #17-009837

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 1'70			2,278.45
JUL 1'70	433.44		
JUL 1'70	576.82		
JUL 8'70	15.64		
JUL 8'70	494.57		
JUL 8'70	582.41		
JUL 15'70	719.43		
JUL 15'70	644.46		
JUL 22'70	7.86		
JUL 22'70	669.48		
JUL 22'70	560.62		
JUL 29'70	27.08		
JUL 29'70	667.20		
JUL 29'70	705.53		
AUG 5'70	26.81		
AUG 5'70	545.93		
AUG 5'70	547.04		
AUG 12'70	507.22		
AUG 12'70	913.71		
AUG 19'70	24.70		
AUG 19'70	597.10		
AUG 19'70	.06		
AUG 19'70	566.99		
AUG 31'70NT	6.67		
SEP 30'70NT	28.32		
NOV 11'70	7.97		
NOV 11'70	45.71		
NOV 11'70	5.84		
NOV 11'70	553.94		
OCT 31'70NT	28.53		
NOV 21'70	10.00		
NOV 30'70NT	23.54		
DEC 31'70NT	28.95		

DEFENDANT'S EXHIBIT 6

CONSOLIDATION
STATEMENT

O K Super Markets, Inc.
1903 South Ervay Street
Dallas, Texas 75215

IN ACCOUNT WITH

Kimbell FORT WORTH Company

P. O. Box 1540
Fort Worth, Texas 76101

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
O K Super Market #3 Account #17-009837			$ 3,543.88
O K Super Market #5 Account #17-009852			$ 2,924.77
O K Super Market #8 Account #17-009878			$ 3,094.40
O K Super Markets #11 Account #17-009936			$ 522.42
O K Super Markets #1 Account #17-010017			$ 1,737.45
O K Super Markets #2 Account #17-010025			$ 2,435.19
O K Super Markets #14 Account #17-010587			$ 4,000.46
TOTAL			$18,258.57

4

STATEMENT

O K Super Markets #5
1208 Dallas, Texas
Account #17-009852

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 1'70			2,118.52
JUL 1'70	67.59		
JUL 1'70	72.21		
JUL 1'70	1,003.26		
JUL 8'70	11.77		
JUL 8'70	1,095.27		
JUL 15'70	31.92		
JUL 15'70	148.42		
JUL 15'70	1,007.85		
JUL 29'70	33.58		
JUL 29'70	279.47		
JUL 29'70	879.15		
AUG 1'70	10.00		
AUG 5'70	33.46		
AUG 5'70	36.11		
AUG 5'70	979.45		
AUG 22'70	36.91		
AUG 22'70	402.48		
AUG 22'70	695.10		
AUG 12'70	39.42		
AUG 12'70	1,187.37		
AUG 19'70	21.78		
AUG 19'70	146.44		
AUG 19'70	874.42		
AUG 31'70INT	6.46		
SEP 30'70INT	25.41		
NOV 11'70	41.03		
NOV 11'70	76.95		
NOV 11'70	1,020.35		
OCT 31'70INT	25.41		
NOV 13'70	60.25		
NOV 13'70	69.33		
NOV 13'70	820.54		

STATEMENT

O K Super Markets #3
Dallas, Texas
Account #17-009837

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 3'70		250.00-	
JUL 3'70		1,185.76-	
JUL 9'70		21.02-	
JUL 10'70		1,080.63-	
JUL 13'70		14.30-	
JUL 17'70		1,021.87-	
JUL 20'70		14.30-	
JUL 21'70		3.61-	
JUL 21'70		6.45-	
JUL 24'70		1,264.03-	
JUL 29'70		5.13-	
JUL 29'70		25.27-	
JUL 31'70		1,010.25-	
JUN 27'70		7.22-	
AUG 7'70		250.00-	
AUG 7'70		1,092.62-	
AUG 10'70		6.13-	
AUG 13'70		68.59-	
AUG 14'70		1,363.89-	
NOV 11'70		617.01-	
JAN 15'71			3,543.88

STATEMENT

O K Super Markets #5
1220 Dallas, Texas
Account #17-009852

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 3'70		1,103.98-	
JUL 3'70		25.77-	
JUL 10'70		1,328.08-	
JUL 13'70		4.94-	
JUL 17'70		1,273.22-	
JUL 20'70		31.93-	
JUL 24'70		844.93-	
JUL 25'70		40.50-	
JUL 29'70		2.19-	
JUL 31'70		1,143.06-	
JUN 27'70		7.32-	
AUG 7'70		1,107.04-	
AUG 10'70		5.80-	
AUG 13'70		25.70-	
AUG 14'70		1,188.19-	
AUG 19'70		2.77-	
AUG 26'70		8.64-	
AUG 29'70		13.74-	
NOV 11'70		1,138.33-	
NOV 19'70		1,050.00-	
NOV 21'70		9.00-	
NOV 24'70		41.52-	
DEC 2'70		1,101.59-	
DEC 11'70		1,053.09-	
DEC 17'70		3.54-	
DEC 16'70		1,188.68-	
JAN 2'71		.41-	
JAN 6'71		45.05-	
JAN 6'71			2,924.77

STATEMENT

O K Super Markets #5
1220 Dallas, Texas
Account #17-009852

IN ACCOUNT WITH

Kimbell FORT WORTH Company

EXHIBIT #5

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
DEC 2'70	54.21		
DEC 2'70	1,006.85		
DEC 2'70	40.52		
DEC 9'70	81.50		
DEC 9'70	83.57		
DEC 9'70	888.02		
NOV 30'70NT	6.88		
DEC 16'70	52.79		
DEC 16'70	46.12		
DEC 16'70	1,089.77		
DEC 31'70NT	5.83		

STATEMENT

O K Super Markets #8
Dallas, Texas
Account #17-009878

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
SEP 19'70	30.00		
SEP 30'70NT	24.58		
OCT 31'70NT	24.79		
NOV 30'70NT	24.99		
DEC 31'70NT	25.20		

STATEMENT

O K Super Markets #8
Dallas, Texas
Account #17-009878

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 1'70			1,565.85
JUL 1'70	21.61		
JUL 1'70	163.81		
JUL 1'70	606.41		
JUL 8'70	138.43		
JUL 8'70	629.54		
JUL 8'70	5.07		
JUL 15'70	160.50		
JUL 15'70	608.62		
JUL 22'70	16.65		
JUL 22'70	178.05		
JUL 22'70	3.63		
JUL 22'70	600.64		
JUL 29'70	5.18		
JUL 29'70	174.86		
JUL 29'70	10.90		
JUL 29'70	744.04		
AUG 1'70	50.00		
AUG 5'70	13.80		
AUG 5'70	163.52		
AUG 5'70	10.12		
AUG 5'70	608.35		
AUG 12'70	6.92		
AUG 12'70	21.63		
AUG 12'70	174.84		
AUG 12'70	11.48		
AUG 12'70	648.35		
AUG 19'70	16.84		
AUG 19'70	174.46		
AUG 19'70	20.50		
AUG 19'70	520.34		
AUG 31'70NT	11.25		

STATEMENT

O K Super Markets #11
Dallas, Texas
Account #17-009936

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 1'70			2,461.49•
JUL 1'70	20.76		
JUL 1'70	422.73		
JUL 8'70	26.75		
JUL 8'70	630.66		
JUL 15'70	577.65		
JUL 22'70	19.22		
JUL 22'70	768.14		
JUL 29'70	35.42		
JUL 29'70	1,198.88		
AUG 1'70	50.00		
AUG 5'70	24.74		
AUG 5'70	300.39		
AUG 12'70	27.08		
AUG 12'70	655.62		
AUG 19'70	583.34		
AUG 31'70NT	2.50		
SEP 19'70	30.00		
SEP 30'70NT	13.12		
OCT 31'70NT	13.33		
DEC 4'70	250.00		
NOV 30'70NT	8.13		
DEC 23'70	125.00		
DEC 31'70NT	4.17		

STATEMENT

O K Super Markets #5
Dallas, Texas
Account 617-009878

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 3'70		758.10-	
JUL 3'70		15.59-	
JUL 10'70		516.53-	
JUL 11'70		9.00-	
JUL 13'70		2.41-	
JUL 17'70		667.28-	
JUL 20'70		24.95-	
JUL 24'70		739.09-	
JUL 25'70		9.00-	
JUL 31'70		791.83-	
JUN 27'70		4.69-	
AUG 5'70		773.04-	
AUG 10'70		20.02-	
AUG 13'70		6.20-	
AUG 14'70		769.12-	
AUG 19'70		18.52-	
JAN 15'71			3,094.40•

STATEMENT

O K Super Market #2
Dallas, Texas
Account #17-010025

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 1'70			1,978.77
JUL 1'70	641.98		
JUL 8'70	29.83		
JUL 8'70	846.47		
JUL 15'70	24.19		
JUL 15'70	637.92		
JUL 22'70	554.89		
JUL 29'70	546.49		
AUG 1'70	50.00		
AUG 5'70	33.89		
AUG 5'70	540.05		
AUG 12'70	10.03		
AUG 12'70	767.03		
AUG 19'70	31.05		
AUG 19'70	699.34		
AUG 31'70NT	6.67		
SEP 19'70	40.00		
SEP 29'70NT	10.83		
OCT 31'70NT	19.58		
NOV 30'70	19.79		
DEC 31'70	19.79		

STATEMENT

O K Super Markets #1
Dallas, Texas
Account #17-010017

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 3'70		734.05-	
JUL 3'70		24.59-	
JUL 10'70		732.51-	
JUL 11'70		1.24-	
JUL 13'70		5.80-	
JUL 13'70		4.60-	
JUL 17'70		808.20-	
JUL 20'70		4.60-	
JUL 20'70		19.30-	
JUL 24'70		798.54-	
JUL 31'70		797.15-	
JUN 27'70		5.20-	
AUG 7'70		797.74-	
AUG 10'70		5.13-	
AUG 13'70		13.33-	
AUG 14'70		753.65-	
AUG 26'70		8.95-	
OCT 1'70		100.00-	
NOV 11'70		780.74-	
NOV 24'70		45.94-	
NOV 24'70		11.95-	
DEC 2'70		649.50-	
DEC 16'70		918.06-	
DEC 18'70		13.52-	
JAN 15'71			1,737.45

STATEMENT

O K Super Markets #1
Dallas, Texas
Account #17-010017

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 1'70			1,297.03•
JUL 1'70	29.44		
JUL 1'70	767.71		
JUL 8'70	19.31		
JUL 8'70	742.43		
JUL 11'70	36.00		
JUL 15'70	33.94		
JUL 15'70	719.72		
JUL 22'70	32.19		
JUL 22'70	541.46		
JUL 29'70	634.01		
JUL 29'70	5.14		
JUL 29'70	7.83		
AUG 1'70	50.00		
AUG 5'70	10.38.		
AUG 5'70	682.32		
AUG 12'70	26.12		
AUG 12'70	744.48		
AUG 19'70	33.37		
AUG 19'70	901.18		
SEP 19'70	40.00		
SEP 30'70NT	15.21		
NOV 11'70	42.02		
NOV 11'70	8.82		
NOV 11'70	52.46		
NOV 11'70	693.08		
OCT 31'70NT	14.37		
NOV 21'70	10.00		
DEC 2'70	16.40		
DEC 2'70	53.40		
DEC 2'70	579.70		
NOV 30'70NT	7.50		
DEC 16'70	67.41		923.23

DEC 16 '70 →

STATEMENT

O K Super Markets #11
Dallas, Texas
Account #17-009936

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 3'70		526.66-	
JUL 9'70		7.84-	
JUL 10'70		519.83-	
JUL 10'70		1,178.67-	
JUL 10'70		250.00-	
JUL 17'70		795.64-	
JUL 17'70		250.00-	
JUL 17'70		3.13-	
JUL 24'70		729.22-	
JUL 31'70		443.49-	
JUN 27'70		4.01-	
AUG 7'70		657.41-	
AUG 10'70		223.00-	
AUG 12'70		577.66-	
AUG 19'70		35.65-	
AUG 19'70		2.34-	
AUG 19'70		8.85-	
AUG 25'70		13.30-	
NOV 3'70		250.00-	
NOV 10'70		125.00-	
NOV 19'70		129.00-	
NOV 25'70		125.00-	
DEC 1'70		125.00-	
DEC 8'70		125.00-	
DEC 16'70		375.00-	
DEC 31'70		125.00-	
JAN 13'71		125.00-	
JAN 15'71			522.48

STATEMENT

O K Super Markets #14
Dallas, Texas
Account #17-010587

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 1'70			2,188.43
JUL 1'70	1,165.20		
JUL 8'70	7.85		
JUL 8'70	996.30		
JUL 15'70	58.31		
JUL 15'70	1,314.38		
JUL 22'70	52.32		
JUL 22'70	1,160.85		
JUL 29'70	15.46		
JUL 29'70	1,082.08		
AUG 5'70	7.72		
AUG 5'70	60.98		
AUG 5'70	1,194.65		
AUG 12'70	24.68		
AUG 12'70	1,200.95		
AUG 19'70	42.61		
AUG 19'70	935.30		
AUG 31'70NT	14.79		
SEP 30'70NT	33.12		
NOV 11'70	53.63		
NOV 11'70	69.25		
NOV 11'70	1,641.04		
OCT 31'70NT	33.32		
NOV 18'70	15.92		
NOV 18'70	27.21		
NOV 18'70	1,265.89		
DEC 2'70	55.97		
DEC 2'70	1,292.67		
DEC 2'70	25.07		
DEC 9'70	56.98		
DEC 9'70	52.50		
DEC 9'70	938.08		
DEC 11'70	36.75		

STATEMENT

O K Super Market #2
Dallas, Texas
Account #17-010025

IN ACCOUNT WITH

Kimbell FORT WORTH Company

WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 3'70		559.10-	
JUL 9'70		13.48-	
JUL 10'70		481.16-	
JUL 13'70		18.18-	
JUL 17'70		685.02-	
JUL 21'70		29.77-	
JUL 24'70		250.00-	
JUL 24'70		595.02-	
JUL 31'70		250.00-	
JUL 31'70		641.98-	
JUN 27'70		4.37-	
AUG 5'70		876.30-	
AUG 14'70		662.11-	
JAN 15'71			2,442.11
AUG 25'70	6.92-		
JAN 15'71			2,435.19

CONSOLIDATION
STATEMENT

O K Super Markets, Inc.
1903 South Ervay Street
Dallas, Texas 75215

IN ACCOUNT WITH

Kimbell FORT WORTH Company
WHOLESALE GROCERS

P. O. Box 1540
Fort Worth, Texas 76101

	DEBIT	CREDIT	BALANCE
O K Super Market #3 Account #17-009837			$ 3,543.88
O K Super Market #5 Account #17-009852			$ 2,924.77
O K Super Market #8 Account #17-009878			$ 3,094.40
O K Super Markets #11 Account #17-009936			$ 522.42
O K Super Markets #1 Account #17-010017			$ 1,737.45
O K Super Markets #2 Account #17-010025			$ 2,435.19
O K Super Markets #14 Account #17-010587			$ 4,000.46
TOTAL			$18,258.57

STATEMENT

O K Super Markets #14
Dallas, Texas
Account #17-010587

IN ACCOUNT WITH

Kimbell FORT WORTH Company
WHOLESALE GROCERS

	DEBIT	CREDIT	BALANCE
JUL 3'70		1,067.55-	
JUL 9'70		63.77-	
JUL 11'70		13.50-	
JUL 13'70		24.51-	
JUL 17'70		1,059.21-	
JUL 24'70		1,408.73-	
JUL 25'70		7.85-	
JUL 29'70		25.14-	
JUL 31'70		1,165.20-	
JUN 27'70		7.65-	
AUG 4'70		5.80-	
AUG 7'70		1,004.15-	
AUG 14'70		1,372.69-	
AUG 14'70		250.00-	
AUG 19'70		30.73-	
AUG 22'70		4.50-	
NOV 11'70		1,763.92-	
NOV 19'70		1,350.00-	
DEC 2'70		1,348.91-	
DEC 11'70		1,446.91-	
DEC 16'70		1,649.99-	
DEC 17'70		5.36-	
DEC 17'70		4.58-	
JAN 6'70		47.40-	
DEC 31'70NT	7.92		
JAN 15'71			4,000.76

This STATEMENT is presented to a filing officer for filing pursuant to the Uniform Commercial Code

1 Debtor(s) (Last Name First) and mailing address

O.K. Super Markets, Inc.
1403 S. Ervay
Dallas, Texas 75215

2 Secured Party(ies) Name and address

Republic National Bank
Pacific & Ervay Streets
Dallas, Texas 75222

3. Maturity Date (if any):

4 For Filing Officer (Date, Time, Number and Filing Office)

SECRETARY OF STATE
FILED 8:30 AM
Feb. 18 JAN 21 19 69

This statement refers to original financing Statement No. 254984 Date Filed

5 A Continuation ☐ The original financing statement is still effective

B Assignment ☒ The secured party of record has assigned his interest in the following collateral to

C Termination ☐ The secured party of record no longer claims a security interest under the Financing Statement

D Partial Release ☐ The secured party of record releases the following collateral

E Amendment ☐ The financing statement is amended as set forth below

(This space, if needed, is for continuation of items B, D and E above)

1309 Main St., Dallas, Texas 75202 All of debtor's machinery, fixtures, and inventory, now existing or hereafter acquired, all replacements and substitutes therefor, all accessions, attachments and additions thereto, and all tools, parts and equipment now or hereafter added to or used in connection with such machinery and equipment, and all similar property hereafter acquired by debtor. Debtor not authorized to dispose of machinery and equipment. Collateralallocated at: 1403 S. Ervay,----continued----------

(FOLD HERE)

Republic National Bank of Dallas

By _____ Signature(s) of Debtor(s)

By (CONTINUED ON NEXT PAGE) Signature(s) of Secured Party(ies)

(2) FILING OFFICER COPY - ACKNOWLEDGEMENT

STANDARD FORM - FORM UCC-3 — Approved by Secretary of State of Texas - Moore Business Forms, Inc., Denton, Texas

This STATEMENT is presented to a filing officer for filing pursuant to the Uniform Commercial Code

3 Maturity Date (if any):

1 Debtor(s) (Last Name First) and mailing address

O.K. Super Markets, Inc.
1403 S. Ervay
Dallas, Texas 75215

2 Secured Party(ies) Name and Address

Republic National Bank
Pacific & Ervay Streets
Dallas, Texas 75222

4 For Filing Officer (Date, Time, Number and Filing Office)

SECRETARY OF STATE
FILED 8:30 AM
JAN. 21 '71

This statement refers to original financing Statement No. 254984 Date Filed Feb 8 Jan 21 1971 19 69

5 A Continuation ☐ The original financing statement is still effective.

B Assignment ☒ The secured party of record has assigned his interest in the following collateral to

C Termination ☐ The secured party of record no longer claims a security interest under the Financing Statement.

D Partial Release ☐ The secured party of record releases the following collateral.

E Amendment ☐ The financing statement is amended as set forth below.

(This space if needed, is for continuation of items B, D and E above)

-----Continuation--------- of Assignment to Small Business Administration
1309 Main Street, Dallas, Texas 75202

6123 Oakland, n4630 Hatcher, 3805-7 E. Kiest Blvd., 3026 Grand Ave., 4121 Colonial, 912 S. Corinth St., 2900 S. Lamar, 1903-19 S. Ervay, 5109 Bexar, 3227 Pennsylvania

(FOLD HERE)

Republic National Bank of Dallas

By _____ Signature(s) of Debtor(s)

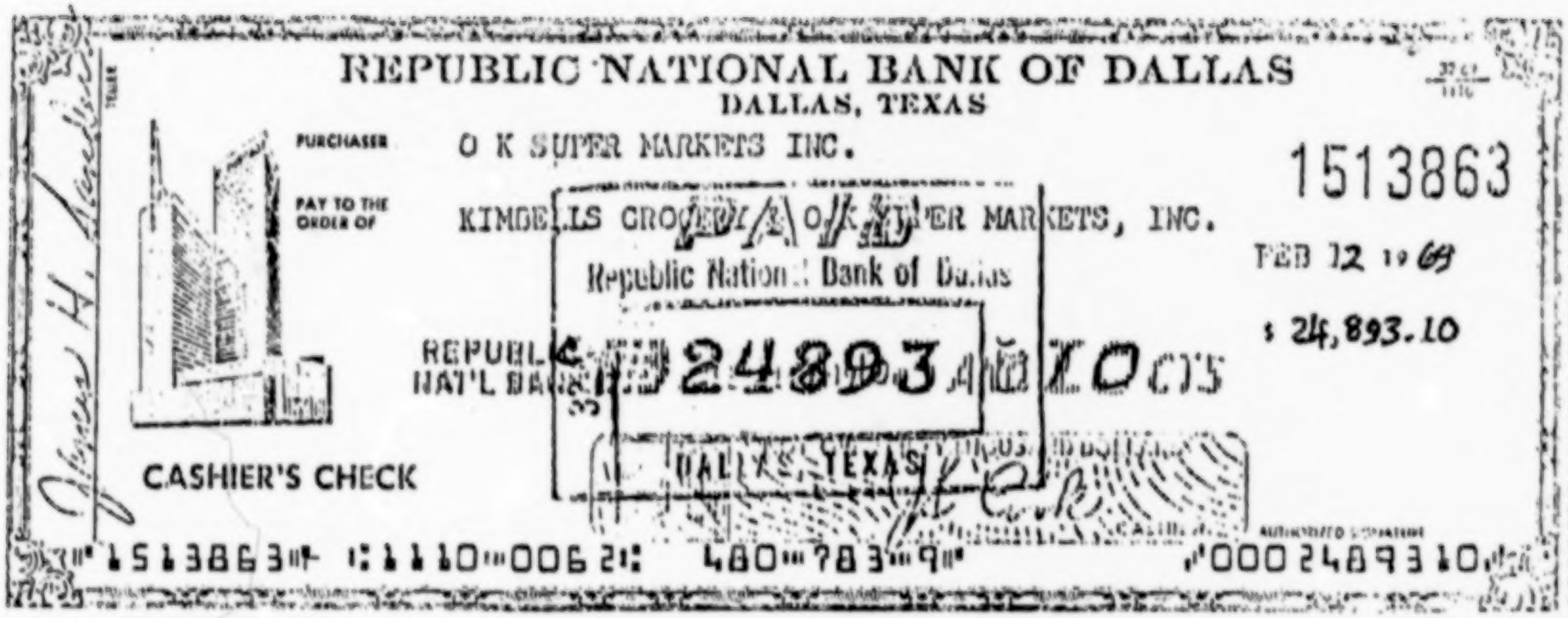
By _____ Signature(s) of Secured Party(ies)

(CONTINUED ON NEXT PAGE)

(2) FILING OFFICER COPY - ACKNOWLEDGEMENT

STANDARD FORM - FORM UCC-3 — Approved by Secretary of State of Texas - Moore Business Forms, Inc., Denton, Texas

DEFENDANT'S EXHIBIT 8


REPUBLIC NATIONAL BANK OF DALLAS
DALLAS, TEXAS

PURCHASER O K SUPER MARKETS INC.

1513863

PAY TO THE ORDER OF KIMBELLS GROCERY & O K SUPER MARKETS, INC.

FEB 12 19 69

$ 24,893.10

REPUBLIC NAT'L BANK 24893 DOLS 10 CTS

PAID
Republic National Bank of Dallas
DALLAS, TEXAS

CASHIER'S CHECK

AUTHORIZED SIGNATURE

⑆1513863⑈ ⑆1110⑉0062⑆ 480⑉783⑉9⑈ ⑈0002489310⑈

O. K. Supermarkets Inc.

KIMBELL'S GROCERY
BY C. T. Oliver
O.T.Oliver

FOR DEPOSIT ONLY TO
THE FORT WORTH NATIONAL BANK
KIMBELL GROCERY COMPANY
0 C0103

PAY ANY [illegible] R.F.D.
TO FT. WORTH NTL BANK
FT. WORTH, TEXAS

FEB 18 69 000-7749

REPUBLIC NATIONAL BANK OF DALLAS 3 3 32-2/1110

DALLAS, TEXAS 69052C10337

PURCHASER O K SUPER MARKETS

1513864

PAY TO THE ORDER OF ROBERT S. CALVERT COMPTROLLER OF PUBLIC ACCTS. AND O K SUPER MARKETS

FEB 12 1969

$3,073.39

REPUBLIC NAT'L BANK $3073 AND 39 CTS

PAID
Republic National Bank of Dallas
FEB 27 1969
32-62
DALLAS, TEXAS

TAX 1-75.1211010

CASHIER'S CHECK

CASHIER

AUTHORIZED SIGNATURE

⑈1513864⑈ ⑆1110⑉0062⑆ 480⑉783⑉9⑈ ⑈0000307339⑈

DEFENDANT'S EXHIBIT 10

O. K. Supermarkets

Harold Kunkel

PAY TO THE ORDER OF
TREASURER, STATE OF TEXAS
FOR DEPOSIT ONLY
JESSE JAMES
STATE TREASURER OF TEXAS
AUSTIN, TEXAS

FEB 26 1969

02 9347

TESTIMONY OF HAROLD KINDLE

• • • •

[44]

HAROLD KINDLE

having been first duly cautioned and sworn to testify the truth, the whole truth and nothing but the truth, [45] did testify as follows:

DIRECT EXAMINATION

BY MR. CABANISS:

Q. Would you state your name, please?
A. Yes, it is Harold Kindle.
Q. All right.
How are you employed, Mr. Kindle?
A. I'm in the real estate business.
Q. How long have you been in the real estate business, Mr. Kindle?
A. Two years.
Q. Prior to that time how were you employed?
A. I was President of O. K. Supermarkets.
Q. And for what period of time, or what general dates, were you President of O. K. Supermarkets?
A. I was President from about '68 to '71.
Q. And prior to 1968, were you employed by O. K. Supermarkets?
A. Yes, sir.
Q. In some other capacity?
A. Yes, sir, I was Vice-President.
Q. For what time, or approximately what dates, [46] were you Vice-President?
A. From about 1956 until 1961.
Q. All right.
Were you active in the management of O. K. Supermarkets during that period covered by your being Vice-President?
A. Yes, sir.

Q. Are you familiar with the various transactions which are the basis for a lawsuit being tried before the Court today?

A. Yes, sir.

Q. Initially, I would like to direct your attention to two of the Plaintiff's Exhibits which have been placed in evidence, these being the Security Agreements; the first one dated August of 1966, and the second April of 1968, and a third in November of 1968.

Are you familiar with each of these three Security Agreements with Kimbell Foods?

A. I'm not sure that I am familiar with the November statement—or, the agreement of '68.

Q. Are you familiar with the other two, August of 1966 and April of 1968, the Security Agreements?

A. Yes, sir.

[47] Q. All right.

Could you tell me what the occasion was for the August, 1966, Security Agreement being entered into?

A. Yes, sir. We were expanding—

Q. (interrupting) Pardon me. When you use the word "we" you ought to identify specifically who you are referring to.

A. Okay. O. K. Supermarkets was expanding and Kimbell assisted us in loaning some money to open up a new store.

Q. Do you remember the sum of money involved?

A. In the twenty thousand range.

Q. I believe the Agreement states a note of $20,000.00.

Now, in what manner was the proceeds from that note, or that sum, utilized by O. K. Supermarkets in opening this store?

A. It was considered as an opening order of merchandise, as well as—in order to place some capital up for other expenditures. They extended us that much credit.

Q. At this time, in 1966, was Kimbell Foods serving as a principal wholesaler in supplying O. K. Supermarkets with inventory?

[48] A. Yes, sir.

Q. By reason of the negotiations as a result of this note and Security Agreement being executed, are you indicating that there was a delay in payment of your account which enabled you to use the current cash flow for purposes of this expansion?

A. Yes, sir, because normally that would cover more than the opening inventory. It is for opening inventory as well as other capital. An opening inventory wouldn't usually run, say, $20,000.00 at one time.

Q. In the absence of having executed this note and Security Agreement would you have been obligated to have been making payments to Kimbell Foods which would have been utilizing your cash flow at that time?

A. Yes.

Q. With reference to the April, 1968, Agreement, I believe that this states that it is securing a $27,000.00 note. Will you state what the situation was at the time of that April, 1968, Agreement?

A. Yes, sir. We had—

Q. (interrupting) Again, when you refer to [49] "we", who do you refer to?

A. O. K. Supermarkets had stopped buying from Kimbells for about six or nine months, and we had gone to Associated Groceries, and that didn't work out too well so we made an agreement to borrow enough money from Kimbells—or enough merchandise—so that we could pay A. G. We had financed some equipment at A. G., as well as the store [sic], and they had advanced us the money so we could pay A. G. all their indebtedness and start buying from Kimbells again.

Q. Was there actually cash outlay, or was this, too, an arrangement where you were able to delay paying on your account with Kimbell and use your cash flow of money for the purpose of paying off the A. G. account?

A. Yes. It was not a cash outlay of money, it was the credit of merchandise.

Q. But was it the same purpose as the earlier transaction to enable you to utilize the current cash income—

A. (interrupting) Yes, sir.

Q. (continuing)—without having to pay on the Kimbell account?

A. Yes.

[50] Q. Now, at the time that these two Security Agreements were entered into by O. K. Supermarkets, the one in August of 1966 and the one in April of 1968, did you intend that O. K. Supermarkets—did O. K. Supermarkets intend that those Security Agreements would cover all other advances and open accounts that existed between you and Kimbell Foods?

MR. VICKERS [Counsel for Plaintiff, Kimbell Foods]: May it please the Court, we would object to the attempt to vary the terms of the Agreement itself. There have been no pleadings in this case that would indicate any trial order or anything that would allow the parties to introduce oral agreements that vary the written Agreement.

THE COURT: Well, this being a non-jury case, I'll overrule the objection.

BY MR. CABANISS:

Q. You may proceed to answer the question, Mr. Kindle.

A. Well, I considered the 1966 Agreement a thing of the past from the 1968 Agreement. I felt like it was, you know, a new beginning, and [51] since we intended to pay the full amount—I realize it was a demand note and they could demand it at any time they wanted to, but we had had a good relationship so it was of no real concern. I didn't stop and ponder about, well, should I do this, or should we do this—O. K. Supermarkets.

Q. All right.

I might address your attention to the fact that there was language in each of these Security Agreements, both the one in August of 1966 and the one in April of 1968, which stated that the Security Agreement covered all indebtedness as well as the specific note that was identified.

Now, with reference to that latter language, I would inquire whether it was your intention that the Security

Agreement would cover from then on advances in the open account, between the two of them?

A. There again, there was not any specific instruction—on this question I mean—about which agreement would cover which. I felt like we signed a new statement in '68, and everything that had transpired in the past was history. I felt like that any monies expended on either one [52] of those, without an abrupt halt and then a start over again, would be—that '66 would be history now, and then when the '68 was paid off it would be history as well.

Q. Now, in 1969, was O. K. Supermarkets able to secure from Republic National Bank, with the participation of the Small Business Administration, a loan in the sum of $300,000.00?

A. Yes, sir.

Q. All right.

Was a portion of that loan used to pay any indebtedness to Kimbell Foods?

A. Yes, sir.

Q. What was the amount that was used in that way?

A. We had two accounts at that time with—

Q. (interrupting) Again, when you say "we"—

THE COURT: (interrupting) You don't need to keep asking him. I know who he is talking about.

THE WITNESS: O. K. Supermarkets had two accounts. There was an open account, and as well as I remember it was about $19,000.00. Then there was this note amount that we had been paying $1,000.00 a month, I [53] believe, plus the interest. So, we actually had two accounts. We had a note amount and an open account.

BY MR. CABANISS:

Q. All right.

A. One was in about nineteen—I believe about nineteen thousand.

Q. Was any payment made on either of them at the time you secured the $300,000.00 loan from Republic Nationai Bank?

A. Yes, we paid off the twenty four thousand, and I believe nine hundred and something, which was $24,000.00 plus the interest.

Q. Was there—

A. (interrupting) Then we agreed to pay, I believe it was $250.00 a week or a month on this other balance, the $19,000.00 on open account, in addition to our regular purchases each week.

Q. Was the amount that was paid the balance remaining at that time, plus the interest, on the $27,000.00 note?

A. Yes, sir.

Q. Now, at the time that either O. K. Super- [54] markets secured the $300,000.00 loan from the Republic National Bank in which the SBA participated, did you have discussions with the personnel of Kimbell Foods concerning the indebtedness that existed at that time between O. K. Supermarkets and Kimbell Foods?

A. Yes, sir.

Q. Were they advised in the course of those conversations what relationship their security, their indebtedness, had with reference to this new loan that you were seeking from Republic Bank?

A. Well, we were trying to work our way out of our difficulties, and I kept them posted on what—see, the application and the other requirements for the loan took several months, and I kept them posted on how we were coming along and when they might be able to expect some relief from their indebtedness.

Q. Did Republic Bank inform you as to what sort of security they would have to have if they were to make this loan, and how it would have to stand with reference to any existing indebtedness you had?

A. Yes, I had to carry the SBA appraiser around [55] to all the stores and let him make an on-sight appraisal of all the equipment and inventory.

Q. And what was to occur with reference to that equipment and inventory insofar as this proposed loan was concerned?

A. We were to consolidate the loans, so to speak, and pay off all the lienholders that we could, pay off all indebtedness that we could, and the Bank and SBA would take a mortgage on all of our equipment and inventory.

Q. Were they taking a first or second mortgage according to the plan for the note?

A. They said that they would require a first mortgage.

Q. All right.

Were representatives of Kimbell Foods with whom you dealt during that period, were they aware of the fact that Republic stated that it would have to have a first mortgage?

A. We discussed generally the terms of the loan. I don't remember a specific conversation when I said, you know, "They had to have a first mortgage, would you release your Security Agreement?" Neither do I remember where they said, "Regardless of what you do, we will not [56] release our Security Agreement."

Q. By the time these negotiations reached the point of the note being approved, the loan being approved and the note executed and disbursement of the proceeds, did you have any understanding yourself as to whether Republic Bank would have a first mortgage upon approving the loan?

A. No, I felt that they would have a first mortgage.

Q. Now, I may have already asked this: Did you state—I believe you indicated the amount paid from the loan to Kimbell Foods. I believe that you had other creditors at that time; is that correct?

A. Yes, sir.

Q. Were these other creditors paid off completely, or were some of them left with indebtedness that was not discharged from the proceeds of that $300,000.00 loan?

A. No, there were a number that were left with indebtedness. Some were paid off fully, some other equipment loans we paid off fully. I believe we got all the taxes current, but some of the other suppliers were still holding—still had balances. We still owed them balances.

[57] Q. Well, when you say "other suppliers," were these people who likewise had open accounts and transactions with you?

A. Yes, sir.

Q. And you state that some of them did have balances remaining that were not discharged?

A. Yes.

Q. All right.

At the time the transactions entered into in 1971 whereby O. K. Supermarkets sold three of their outlets and the sale from which the funds are involved in this case, was there any other creditor that O. K. Supermarket had at that time other than Kimbell Foods who had to agree to these sales in order for them to be carried out?

A. No, sir.

Q. There is, as one of the items of evidence that was introduced by Plaintiff, an Agreement that was entered into in February of 1971 concerning how the proceeds from these sales would be delivered to Republic Bank and held by Republic in an escrow account. Was that arrangement a matter in which you participated as one of the individuals representing the O. K. [58] Supermarkets?

A. Yes, sir.

Q. One paragraph of the Agreement includes a statement that the fund would be held subject to creditors' claims being considered against it. Are you able to state what creditor or creditors were being considered by the Republic to that Agreement at the time it was made?

A. No, I felt that there would be a number of creditors because we owed quite a few other people, and the situation was deteriorating rapidly. We didn't know what suits might come up later on, and we felt that this was the best solution, and let the Courts decide.

Q. Were there any suits at that time?

A. Not that I know of.

Q. In 1971?

A. No, sir.

Q. When was it that Kimbell Food introduced a suit against O. K. Supermarkets in the State Court in Tarant County?

A. I don't have that. I am aware that they did, but I don't have the date.

Q. Were you aware that such litigation either existed at that time, or might result at the time [59] this Agreement was entered into?

A. Yes. I think it had already been—before this Agreement was worked out, it had already been filed.

Q. Now, you mentioned that there were other creditors that you thought might have a claim to assert. What type of creditors are you referring to?

A. Just general suppliers; milk companies, bread companies, produce companies.

Q. Were you aware at that time that any taxing authorities, such as the City of Dallas or the State of Texas, would have claims that they might assert?

A. Our bookkeeping system had broken down then and I really wasn't aware—really wasn't aware of what taxes had been paid as they accrued, and the ones that hadn't.

MR. CABANISS: Pass the witness.

CROSS EXAMINATION

BY MR. VICKERS:

Q. Mr. Kindle, in connection with the exhibits [60] which have been marked as Plaintiff's Exhibits 1, 2 and 3—

MR. VICKERS: With the Court's permission, if I could approach the witness stand so he will be aware of these exhibits that I am referring to.

THE COURT: All right.

BY MR. VICKERS:

Q. Mr. Kimbell, Plaintiff's Exhibit 1, 2 and 3 that I have just shown you, those were copies of the Financing Statements and Security Agreements of Kimbell Foods?

A. Yes.

Q. You did not at any time make a request of anyone at Kimbell Foods for a release or a termination

statement in reference to those Financing Statements or Security Agreements, did you?

A. No, sir.

Q. Now, you were represented—Did your company have an attorney representing you?

A. Yes, sir.

Q. Mr. Tom James?

[61] A. Yes, sir.

Q. You didn't request of Mr. James that he secure from Kimbell Foods—

A. (interrupting) No.

Q. (continuing)—a release or termination of any of these agreements at any time?

A. No, sir.

Q. Now, when you got—or began to make arrangements for the loan with the Republic Bank, did you inform them that there was outstanding a first lien or Security Agreement that Kimbell Foods had?

A. Yes, sir.

Q. So that they were aware of that when you obtained the $300,000.00 loan?

A. I say "yes, sir." We had to give a detailed financial statement on everyone that we owed money to and the amount, and I am sure theirs was included in that statement.

Q. Now, you mentioned in connection with the investigation that the SBA made, that they had an appraiser come out. Do you know what value he appraised your property for in connection with that loan?

A. No, sir.

[62] Q. Do you know whether it was in excess of $300,000.00?

A. I don't really know.

Q. Do you have any way of saying whether it was in excess of the amount that was owed to the Plaintiff at that time?

A. I'm sure, yes, sir, that it was.

Q. Now, isn't it true that when this loan was originally discussed that the Bank wanted the creditors to guarantee a portion of that loan?

A. Yes.

Q. Did you talk with someone at the Plaintiff about that?

A. Yes, sir.

Q. Was that Mr. Kidwell?

A. Yes, sir.

Q. Did Mr. Kidwell inform you that Kimbell Foods would not agree to guarantee any portion of that loan?

A. Yes, sir.

Q. Now, in reference to the payment that you testified to that was made to Kimbell in the amount of approximately $24,000.00.

A. Yes, sir.

Q. At that time—at the time that that payment [63] was made was that money given to you by the Bank?

A. The checks were given to—We gave them a list of the amounts and the people that they were to go to, and I think they gave the checks to me and I believe I mailed them. I am not really sure.

Q. Who at the Bank gave you those checks?

A. Dan Davis.

Q. At the time that Mr. Davis gave you that check, had you given to him any releases or termination agreements from anyone in connection with the Plaintiff?

A. No, sir.

Q. Did he furnish to you any copies of any agreements to obtain from them?

A. No, sir.

Q. When you delivered those checks—that check to the Plaintiff, did you at the time of the delivery of that check request from them, in exchange for that check payment, a copy of a release or a termination agreement?

A. No, sir.

Q. In fact, as you stated, you believed that you mailed that check, and in mailing that check you made no request for a termination agreement [64] or release?

A. No, sir.

Q. No, you—

A. (interrupting) No, I didn't make a request.

Q. Now, you did make mention about something that you thought that after the 1966 you were beginning anew and that these older Financing Statements and Security Agreements were history. Nobody ever told you that that was true from Kimbell did they?

A. No, sir.

Q. Nor did your own attorney, Mr. James, tell you that?

A. No.

MR. VICKERS: That is all the questions I have, Your Honor.

THE COURT: Mr. McMasters?

MR. McMASTERS: No questions, Your Honor.

MR. JACOB: No questions, Your Honor.

THE COURT: All right.

You may step down.

(Witness excused.)

THE COURT: Any more witnesses?

R. CABANISS: No further witness, * * *

* * * *

SUPREME COURT OF THE UNITED STATES

No. 77-1359

UNITED STATES, PETITIONER

v.

KIMBELL FOODS, INC., et al.

ORDER ALLOWING CERTIORARI

Filed May 15, 1978

The petition herein for a writ of certiorari to the United States Court of Appeals for the Fifth Circuit is granted.

☆ U. S. GOVERNMENT PRINTING OFFICE: 1978 288659 58

77-1359

NO.

IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1977

UNITED STATES OF AMERICA, PETITIONER

v.

KIMBELL FOODS, INC., ET AL

REPLY TO PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

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1025 Elm Street
Dallas, Texas 75202

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OCTOBER TERM, 1977

UNITED STATES OF AMERICA, PETITIONER

v.

KIMBELL FOODS, INC., ET AL

REPLY TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

QUESTION PRESENTED

Whether a contractual lien duly perfected in accordance with state law may be defeated by a subsequent contractual lien in favor of an agency of the federal government.

STATEMENT

On or about August 4, 1966 O K Super Markets, Inc. granted to Kimbell Foods, Inc. a security interest in certain equipment, goods, wares and merchandise to secure a promissory note from Kimbell Foods, Inc. In connection therewith a financing statement was duly filed with the Secretary of State of Texas on September 2, 1966 along with a copy of the underlying security agreement and a list of the collateral.

On April 17, 1968 and November 7, 1968 O K Super Markets, Inc. executed additional security agreements and financing statements in favor of Kimbell Foods, Inc. which were cumulative of each other and

were in addition to an extension of the security agreement and financing statement dated August 4, 1966. These security agreements with attached lists of collateral and financing statements for each were also duly filed with the Secretary of State of Texas on April 22, 1968 and November 21, 1968 respectively.

Each of the security agreements executed by O K Super Markets, Inc. in favor of Kimbell Foods, Inc. provided that the security interest granted was to secure the therein-described promissory notes and in addition was also given to secure payment of all other indebtedness at any time thereafter owing by O K Super Markets, Inc. to Kimbell Foods, Inc.

On February 12, 1969 O K Super Markets, Inc. executed in favor of Republic National Bank of Dallas a security agreement and financing statement providing for a security interest in all of the O K Super Markets, Inc.'s goods, inventory, fixtures and equipment then existing or thereafter acquired. On the same date Republic National Bank loaned O K Super Markets, Inc. $300,000.00 which loan was 90% guaranteed by the Small Business Administration. Part of the proceeds of such loan were used to pay Kimbell Foods, Inc. a remaining balance due on a promissory note owing to Kimbell Foods, Inc. However, there still remained an amount of $18,390.93 owing to Kimbell Foods, Inc. by O K Super Markets, Inc. upon an open account indebtedness, such indebtedness having been accrued for merchandise sold to O K Super Markets, Inc. as of February 12, 1969.

No termination statement was filed by Kimbell Foods, Inc. as to any of the

financing statements described above nor was any requested of Kimbell Foods, Inc.

On or about February 18, 1969 a financing statement was filed with the Secretary of State of Texas naming O K Super Markets, Inc. as debtor and Republic National Bank of Dallas as secured party. Said financing statement provided for a security interest in all of the debtor's goods, inventory, fixtures and equipment then existing or thereafter acquired. The face of the financing statement did not indicate in any manner the participation by the Small Business Administration nor were any other writings filed.

On January 15, 1971 Kimbell Foods, Inc. filed suit against O K Super Markets, Inc. in the 96th District Court of Tarrant County, Texas for the net amount of $18,258.57 principal, plus costs and attorneys' fees and joined Republic National Bank as a defendant. Republic National Bank was thereafter removed as a defendant and the cause as to it was transferred to the District Courts of Dallas County, Texas.

On or about February 3, 1971 the Small Business Administration of the United States of America paid to Republic National Bank of Dallas 90% of O K Super Markets, Inc.'s indebtedness to the Republic National Bank of Dallas which was in the amount of $252,331.93 and was assigned a proportionate interest in the security interest held by Republic National Bank of Dallas in the property of O K Super Markets, Inc. On or about January 21, 1971 a financing statement was filed with the Secretary of State of Texas by the Small Business Administration reflecting the assignment set

forth above.

On or about February 3, 1971 Republic National Bank and O K Super Markets, Inc. entered into an agreement approved as to form and substance by Kimbell Foods, Inc. and the Small Business Administration whereby collateral covered by the security agreement and financing statements of Kimbell Foods, Inc. was sold and the proceeds of such sale were to be held in escrow by Republic National Bank to be paid over to the party or parties entitled to such proceeds after appropriate determination by court proceedings.

On February 4, 1972 a judgment was entered in the 96th District Court of Tarrant County, Texas for Kimbell Foods, Inc. against O K Super Markets, Inc. granting judgment to Kimbell Foods, Inc. on its claims against O K Super Markets, Inc.

On or about May 4, 1972 Kimbell Foods, Inc. filed an original complaint in the United States District Court for the Northern District of Texas, Dallas Division against Republic National Bank of Dallas and United States of America, defendants, requesting that the court find Kimbell Foods, Inc.'s claim to the proceeds of the property of O K Super Markets, Inc. sold pursuant to the agreement of February 3, 1971 prior and superior to the claims asserted by the defendants.

On July 15, 1974 the case went to trial and on October 1, 1975 a judgment was filed ordering that Kimbell Foods, Inc. was not entitled to any portion of the sum held in escrow by Republic National Bank of Dallas pursuant to the agreement of February 3, 1971 and denying the relief sought by Kimbell Foods, Inc. against

Republic National Bank of Dallas and the United States of America.

The Court of Appeals reversed the holding of the District Court rejecting the choateness doctrine adopted by the District Court in determining the priority of conflicting security interests between contractual lenders in the private sector and agencies of the federal government engaged in commercial lending.

REASONS FOR DENYING THE PETITION

In urging a uniform approach for determining the priorities of competing liens in cases involving the federal government, petitioner commits a sin of omission in failing to distinguish between those cases involving liens which vary significantly from state to state and those cases involving liens for which a uniform national means of resolution already exists.

In illumination of its premise that the choateness doctrine should be applicable to competing liens in situations involving the federal government, petitioner presents cases where the federal lien was invariably founded upon expressed statutory authority ascribing priority to the federal lien in relation to competing non-federal liens. Moreover, the competing non-federal liens in each such instance were of a nature that varies from state to state, such as mechanic's and materialman's liens.

The case at hand is clearly distinguishable in that it involved the resolution of conflicting security interests between contractual lenders, each of which had sought to protect their security interests in accordance with state law patterned after

the Uniform Commercial Code.

The Court of Appeals has formulated a well reasoned approach for the resolution of competing security interests between contractual lenders in the private sector and agencies of the federal government engaged in commercial lending. As was recognized in Chicago Title Insurance Company, et al v. Sherred Village Associates, 568 F. 2d 217, 222 (1st Cir., Jan. 5, 1978), the application of the Uniform Commercial Code to competing privately-held security interests was an admirable device since "the Uniform Commercial Code is of general nationwide application with no quixotic parochial variations".

The Uniform Commercial Code is designed to promote and stabilize interstate commerce by providing a nationally uniform and consistent codification of accepted commercial principles. All states, with the exception of Louisiana, have adopted the Uniform Commercial Code, and Article 9 of the Uniform Commercial Code is in effect on a nationwide basis without any material alterations or modifications.

The application of Article 9 of the Uniform Commercial Code to situations such as the case at bar provides a proven, accepted, and equitable means of uniformly resolving such conflicts without prejudice to any segment of the national lending sector.

Under the approach taken by the Court of Appeals, the United States is able to rely upon a uniform policy governing priorities between competing lien creditors, and when engaging in commercial lending through any of its agencies, the federal government is as able as any other commercial lender to evaluate its credit risks prior to making loans.

To reject the application of Article 9 of the Uniform Commercial Code in instances such as this would thwart the national policies underlying the Uniform Commercial Code and would be a repudiation of the legislative wills of the peoples of all states which have adopted Article 9 of the Uniform Commercial Code.

A second and equally compelling reason exists for rejecting the petitioner's petition for a writ of certiorari. If the approach to future similar situations espoused by petitioner were applied, it is highly unlikely that any prior private creditor could prevail against the United States unless the amounts due and owing to that private creditor were first reduced to judgment.

It is respectfully submitted that if private lenders having duly perfected their security interests under the Uniform Commercial Code were faced with the prospect of having their security defeated by a subsequent contractual lien acquired by an agency of the federal government, then lending activities in the private sector of the economy would be drastically curtailed resulting in a significant diminishment of funds available to small entrepreneurs.

Funding from the private sector is absolutely essential to the growth and well being of small enterprises.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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Foods, Inc.

HOLT GUYSI
Attorney for Kimbell
Foods, Inc.

APRIL 1978.

No. 77-1359

In the Supreme Court of the United States

OCTOBER TERM, 1978

UNITED STATES OF AMERICA, PETITIONER

v.

KIMBELL FOODS, INC., ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES

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ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-29a)[1] is reported at 557 F.2d 491. The opinion of the district court (Pet. App. 31a-51a) is reported at 401 F. Supp. 316.

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[1] "Pet. App." refers to the Appendix to the Petition for Certiorari.

JURISDICTION

The judgment of the court of appeals (Pet. App. 30a) was entered on August 12, 1977. A timely petition for rehearing was denied on October 25, 1977 (Pet. App. 54a). On January 16, 1978, Mr. Justice Powell extended the time within which to file a petition for a writ of certiorari to and including March 24, 1978. The petition was filed on that date and was granted on May 15, 1978 (App. 103). The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether a private lien that has not attached to the property and become choate before a federal lien attaches takes precedence over the federal lien.

STATEMENT

1. Respondent Kimbell Foods, Inc., filed this suit seeking a determination that its security interest in certain personal property of O.K. Super Markets, Inc., was prior and superior to a security interest in that property held by the Small Business Administration (SBA) and the Republic National Bank of Dallas (App. 15).

O.K. Super Markets, Inc. ("O.K."), a Dallas supermarket chain, became indebted to Kimbell Foods ("Kimbell"), a grocery wholesaler, as a result of inventory purchases. In August 1966, in order to help O.K. open a new store, Kimbell extended $20,000

credit to O.K. (App. 92). The debt was evidenced by a $20,000 promissory note and was secured by a Security Agreement and Financing Statement, filed with the Texas Secretary of State on September 2, 1966 (App. 9, 16-18). The collateral listed in the agreement included grocery store equipment and fixtures and "[a]ll goods, wares and merchandise and any and all additions or accessions thereto" (Pet. App. 2a; App. 9, 16-18). The agreement also contained a printed "dragnet" clause stating that "said security interest [is] also being given to secure the payment of all other indebtedness at any time hereafter owing by Debtor to Secured Party as well as the discharge of all obligations imposed upon Debtor hereunder" (App. 17).

In April and November, 1968, O.K. and Kimbell entered into two additional security agreements securing a single $27,000 note from O.K. This loan permitted O.K., which in the interim had changed to another supplier, to pay off that company and return to Kimbell (App. 92-94). These agreements, which were filed with the Texas Secretary of State on April 22 and November 21, 1968, also contained the dragnet clause securing future advances by Kimbell to O.K. (App. 19-21, 22-25).

During the latter part of 1968, O.K. sustained substantial losses because of a boycott (Pet. App. 34a; App. 62). O.K. therefore sought a $300,000 loan from the Republic National Bank of Dallas and applied to the SBA for a guarantee of the loan (Pet. App. 34a; App. 62). The Bank and the SBA tried

to get Kimbell and O.K.'s other creditors to guarantee portions of the loan, but were unsuccessful (Pet. App. 34a; App. 61-64).[2]

The Republic National Bank made the loan to O.K. on February 12, 1969. To secure O.K.'s note for $300,000 (which was designated by "SBA Loan No." and executed on an SBA form (App. 70-71)), O.K. executed a Security Agreement and Financing Statement in favor of the Bank (App. 67-69). The listed collateral, in which the Bank was given a security interest, was "[a]ll the debtor's machinery, fixtures, equipment and inventory, now existing or hereafter acquired, * * *" located at specified addresses (App. 67-68; see App. 47-48, 70-71; Pet. App. 34a). The financing statement covering the collateral was filed with the Texas Secretary of State on February 18, 1969 (App. 69).[3]

The SBA guaranteed 90 percent of the loan by Republic National Bank to O.K. (App. 48, 72-75).[4] It did so under the authority granted by Section 7(a)

[2] Kimbell, along with other major creditors of O.K., was asked to guarantee a *pro rata* share of the loan, based on the amount O.K. owed Kimbell, in return for payment in full of its account. Kimbell declined to do so, noting in an internal memorandum that it did not want to become contingently liable as a method of collecting debts and that "we want our account paid in full before we release our security" (App. 61-64).

[3] O.K. had previously delivered to Republic National Bank a financing statement covering collateral of a similar description (App. 26, 47), but there was no loan outstanding at that time.

[4] The Bank represented to the SBA that $200,000 of the loan would be used for debt payment and the remainder for "working capital," primarily to purchase inventory (App. 72).

of the Small Business Act, 72 Stat. 387, as amended, 15 U.S.C. 636(a) (App. 72). That provision authorizes loans to small business concerns where "financial assistance * * * is not otherwise available on reasonable terms from non-Federal sources" (15 U.S.C. 636(a)(1)).

In February 1969, when the SBA-guaranteed loan was executed, O.K. owed Kimbell $24,893.10 on the 1968 note, and proceeds from the loan were used to pay off this balance (Pet. App. 3a; App. 47, 48, 60).[5] O.K. at that time also owed Kimbell $18,390.93 on open account (App. 47, 76-84). O.K. subsequently made payments in excess of that amount, and the payments were credited against the oldest outstanding charges, thereby discharging this debt (Pet. App. 4a; App. 48-49, 76-84). O.K. continued to purchase from Kimbell, and, by January 15, 1971, there was a new balance of $18,258.57 on open account (Pet. App. 4a; App. 48-49, 76-84).

On January 15, 1971, Kimbell filed suit against O.K. in the 96th Judicial District Court of Tarrant County, Texas, to foreclose its security interest and recover the unpaid balance of $18,258.57, plus interest, contractual and statutory attorneys' fees, and costs (App. 11-12, 49). Shortly before, O.K. had defaulted on the SBA-guaranteed loan, and Republic National Bank, on December 30, 1970, had therefore assigned its security interest to the SBA (App. 49-50, 67, 70). On February 3, 1971, the SBA paid the

[5] There was no other promissory note between O.K. and Kimbell outstanding, the 1966 note having also been disposed of (Pet. App. 3a-4a and n.2; App. 47).

Bank 90 percent of O.K.'s outstanding indebtedness, which totaled $252,331.93 (App. 49-50, 67, 70). The assignment from the Bank to the SBA was filed with the Texas Secretary of State on January 21, 1971 (App. 50, 86).

In early February, 1971, O.K.'s creditors—the Bank, the SBA, and Kimbell—signed an agreement with O.K. providing that three of O.K.'s stores would be sold in bulk and the proceeds of the sale placed in escrow pending resolution of competing claims to the funds (App. 49).[6]

Approximately a year later, on February 4, 1972, the state court entered judgment for Kimbell Foods against O.K. Super Markets in the sum of $24,445.37 (Pet. App. 33a, n.2).[7]

2. Kimbell then filed the present suit in the United States District Court for the Northern District of Texas, pursuant to 28 U.S.C. 2410,[8] seeking a declaration that its security interest in O.K.'s property created a claim to the escrow fund superior to the claims of the Bank and the United States, and asking for

[6] As of September 15, 1975, $100,836.03 was held in escrow under the agreement (Pet. App. 53a).

[7] This amount consisted of $18,258.57 principal, $1,186.80 interest, and statutory attorneys' fees of $5,000 (Pet. App. 33a, n.2; App. 27-29).

[8] That statute provides that the United States may be named a party in suits brought to quiet title to property, or foreclose liens on property, in which the United States has an interest.

judgment against the Bank as custodian of the escrow fund.[9]

The district court held that the United States' security interest was superior (Pet. App. 36a-46a). The court concluded that, under the applicable federal law, a private lien is not entitled to priority over a federal lien unless the private lien has attached to the property, and all opportunities for judicially contesting the amount of the lien have been exhausted, before the federal lien attaches (Pet. App. 36a-42a). Because Kimbell's lien was not "choate" under this standard until February 1972, when Kimbell reduced its lien to judgment, it could not prevail over the security interest of the United States, whose priority dated from the filing of the security agreement by the Republic National Bank in February 1969 or, at the latest, from January 1971 when the Bank's assignment to the SBA was filed (Pet. App. 43a).[10]

3. The court of appeals reversed (Pet. App. 1a-29a). It agreed with the district court that the pri-

[9] The State of Texas and the City of Dallas intervened, claiming delinquent sales taxes and ad valorem taxes from the fund. The district court held that these claims did not qualify for the statutory priority over SBA liens that is provided to claims for state and local property taxes by 15 U.S.C. 646 (see n. 39, *infra*), and that the claimants had no rights against the escrow fund in any event (Pet. App. 46a-51a). The intervenors did not appeal.

[10] The court held alternatively that, as a matter of state contract law, the future-advances or "dragnet" clauses in the agreements securing O.K.'s notes to Kimbell in 1966 and 1968 did not secure the debts arising from the purchases subsequently made by O.K. on open account (Pet. App. 43a-46a).

ority of the federal lien is governed by federal law, but it rejected the "choateness" rule followed by the district court for determining when a lien is deemed to be perfected in competition with a federal lien (Pet. App. 13a-14a). It rejected the choateness rule because it thought that that rule, which was developed largely in connection with federal tax liens, should not be "extended" to situations where the federal government, instead of being the involuntary creditor of tax delinquents, voluntarily makes "garden-variety commercial loans or guaranties" (Pet. App. 17a-19a). The court viewed the collection of debts owed the SBA as "less central" to the proper functioning of the federal government than the collection of tax revenues (Pet. App. 18a-19a).

The court also concluded that adherence to the choateness doctrine would cause potential creditors of businesses eligible for Small Business Administration loans to "shun [those businesses] as anathema," thereby harming the companies that Congress wished to assist and undermining the policy expressed by Congress in establishing the SBA (Pet. App. 19a). Finally, the court observed that Congress in the Federal Tax Lien Act of 1966 "substantially pared the applicability of the choateness doctrine" to tax liens, and reasoned that "logical symmetry" required that the doctrine should not be applied to federal contractual liens (Pet. App. 20a-22a).[11]

[11] The court of appeals also rejected the district court's alternate holding (Pet. App. 43a-46a; see p. 7, n. 10, *supra*) that Kimbell's lien could not have priority because the parties did not intend to cover future indebtedness for inventory purchases under the dragnet clauses of the 1966 and 1968 security agreements. The court of appeals held that under Texas law, "a further extension of credit to the debtor by the lender is deemed future indebtedness reasonably contemplated by the parties when they execute a future advance clause" (Pet. App. 4a-10a). It also concluded that the SBA, standing in the shoes of the Bank, did not have priority on other theories under state law (Pet. App. 10a-13a). We do not present these questions of state law for decision by this Court.

The court of appeals then fashioned a new federal rule for determining priorities. It accepted the established federal rule that the lien "first in time is first in right."[12] But, in place of the choateness test for determining when a non-federal lien arises, it held that a lien that meets the standards of the Uniform Commercial Code (U.C.C.) qualifies to compete for "first in time" with a federal lien (Pet. App. 24a-26a).

The court applied a separate analysis, however, to the question whether the future-advances clauses in the 1966 and 1968 security agreements between O.K. and Kimbell gave the advances made by Kimbell from 1969 to 1971 a security interest with a priority dating back to the 1966 and 1968 agreements. The court considered that the SBA's lien attached when the Republic National Bank's lien arose in February 1969, so that the subsequent advances by Kimbell

[12] The Fifth Circuit has subsequently decided to abandon the "first in time, first in right" rule, at least in the case of mechanics' liens. *United States* v. *Crittenden*, 563 F.2d 678. The United States has filed a petition for a writ of certiorari in *Crittenden* (No. 77-1644). (We have furnished a copy of that petition to counsel for respondents.)

would have priority only if they related back to the dates of the 1966 and 1968 agreements (Pet. App. 26a). Texas law under the U.C.C. would allow relation-back, the court concluded (Pet. App. 12a-13a, 27a), but before the U.C.C., state courts had applied at least three rules concerning whether an optional future advance would relate back to take priority from the date of the original security agreement. Some held that such advances did not relate back, others allowed relation-back unless the advancing creditor had actual notice of the intervening lien, and still others allowed relation-back in all cases (Pet. App. 26a-27a). The court rejected the first of these three rules and found it unnecessary to choose between the last two, since under either of them the court believed that Kimbell's lien for the subsequent advances would relate back to the prior security agreements (Pet. App. 27a-28a).

SUMMARY OF ARGUMENT

This case involves the relative priority of a federal contractual lien, securing a loan guaranteed by a federal agency, and a private lien securing optional advances that were made after the federal loan guarantee was given and the federal lien attached. We contend that because the private lien securing the advances was not specific and perfected—was not "choate"—when the federal lien attached, the federal lien was "first in time" and takes precedence over the subsequently perfected private lien.

1. As the court below recognized, federal law governs the relative priority of federal liens, including the Small Business Administration lien at issue here. In a series of cases involving federal tax liens, this Court has fashioned rules to determine the relative standing of federal liens and competing liens where no Act of Congress does so. Those rules are that the lien "first in time is first in right," and that the time a non-federal lien arises for the purpose of this competition is the time it becomes "choate." A lien is choate when the identity of the lienor, the property subject to the lien, and the amount of the lien are established. *United States* v. *Security Trust & Savings Bank*, 340 U.S. 47; *United States* v. *City of New Britain*, 347 U.S. 81.

The reasons given by this Court for applying the first-in-time and choateness rules in the context of federal tax liens apply with equal force in the context of federal contractual liens. It is equally important to insure the prompt and certain collection of federal revenues whether those revenues arise from taxes or from the payment of contractual debts due the federal government. A dollar received in the Treasury from one source is as useful as a dollar received from the other. This Court's decisions interpreting the federal government's priority under the insolvency statute (R.S. 3466, now 31 U.S.C. 191), where the choateness test originated, have applied the test equally to tax debts and contractual debts. Recovery on loans and guarantees is particularly important to the congressional scheme for the

Small Business Administration, since amounts recovered go into a revolving fund in the Treasury that serves as the source of new loans and guarantees.

A second reason the Court has cited for applying the choateness rule with respect to tax liens is that "[o]therwise, a State could affect the standing of federal liens, contrary to established doctrine, simply by causing an inchoate lien to attach at some arbitrary time even before the amount of the tax, assessment, etc., is determined." *United States* v. *City of New Britain*, *supra*, 347 U.S. at 86. The Court thus recognized that state law is not free to defeat a vested federal property interest, and that some federal test is needed to determine the "time" of a competing lien for the purpose of deciding which lien is "first in time." The same is true with respect to federal contractual liens.

2. Recognizing these considerations, the lower federal courts have proceeded to apply in connection with federal contractual liens the rules that this Court developed in connection with federal tax liens. Prior to enactment of the Federal Tax Lien Act of 1966—which limits the choateness doctrine in the context of federal tax liens—all five of the courts of appeals that considered the question agreed that the rules of first-in-time and choateness were applicable in connection with federal contractual liens. Since enactment of the Federal Tax Lien Act of 1966, at least four courts of appeals have reached the same conclusion, rejecting the argument that that Act has any

bearing on the relative priority of federal non-tax liens.

But the court below, together with the Ninth Circuit, has disagreed. The Fifth Circuit has concluded that the Federal Tax Lien Act of 1966, by modifying the choateness doctrine with respect to federal tax liens, impels the federal courts to abandon that doctrine with respect to federal non-tax liens.

This conclusion is erroneous. In passing the 1966 Act, Congress deliberated and acted only with respect to tax liens, adopting detailed rules governing the relative standing of federal tax liens as against specific categories of competing liens. Nothing in the content or background of the Act suggests any intent to affect the priorities of other kinds of federal liens, particularly on a wholesale and undifferentiated basis. There is, in fact, specific evidence of an intent to leave such questions "to another day." Moreover, in the 1958 amendment to the Small Business Act, Congress focused specifically on the priority of contractual liens held by the Small Business Administration, and diminished those priorities in only a precise and limited way.

3. The additional "policy reasons" given by the court below for rejecting the choateness rule do not withstand scrutiny. The Small Business Administration is not the equivalent of an ordinary "commercial lender." Government loans and guarantees are provided for reasons of national policy, not to make a profit. Loans and guarantees of the Small

Business Administration, like most federal financial assistance, are provided only if commercial credit is not available on reasonable terms. Far from "enter[ing] the commercial credit scheme" with the same "opportunity to evaluate the credit risks" as a private lender (Pet. App. 18A), the government enters only where private lenders do not go. And the choateness rule provides appropriate protection for government loans where the government is the lender of last resort.

4. Stability of legal rules is especially important in commercial law, where "presumably, individuals may have arranged their affairs in reliance on the expected stability of decision." *Monell* v. *Department of Social Services*, No. 75-1914, decided June 6, 1978, slip op. 39. The court below lacked justification for overthrowing the settled law that the courts of appeals had developed concerning the relative priority of federal contractual liens. Indeed, when the Small Business Administration entered into the loan guarantee whose priority is at issue here, the Fifth Circuit itself appeared to follow what was then the unanimous rule in the courts of appeals. The federal government and other parties stand to lose substantial sums, not only in this case but in hundreds of others, if their justified reliance on the choateness doctrine and the first-in-time rule proves to have been incorrect.

5. Moreover, in contrast to the coherent and well-established body of precedent that the court of appeals rejected, the new priority rules it has set out to develop on a case-by-case basis would be virtually

impossible to predict and rely on. The unpredictability of such judicial law-making in this area is well illustrated by the Fifth Circuit's process of choosing the legal rules it would apply in determining the priority of the private lien at issue in this case—and by the questions that the court expressly left open "for another day."

Given the uncertainties arising from any attempt to develop new priority rules through litigation, it is preferable, as other courts of appeals have recognized, to leave such a task to Congress. Congress can consider and determine the relative merits of various categories of federal contractual liens and various categories of competing liens. Congress can modify the choateness rule, if so advised, in a way that assures national uniformity and predictability; and Congress can make the new rules prospective only, if that is considered desirable to protect justified reliance on past rules. Moreover, if a decision is to be made to diminish federal property interests and relinquish federal revenues, in the asserted interest of fairness to competing lienors, Congress should make that decision. Until Congress acts, the first-in-time and choateness rules, which have proved clear and workable and have provided appropriate protection for federal liens, should be applied by this Court with respect to federal contractual liens as they were with respect to federal tax liens.

6. Applying those rules to this case, the lien of the Small Business Administration arising from its guarantee of the loan by the Republic National Bank

takes precedence over the lien of Kimbell Foods for its optional future advances. The court of appeals correctly ruled that the SBA's lien attached in February 1969, when the Bank's security interest was recorded; and at that time Kimbell's lien for the future advances was inchoate, since the advances had not yet been made. But even if the SBA's lien did not attach until January 1971, when the note was assigned to the SBA by the Bank and this assignment was recorded, the SBA's lien is still senior; for Kimbell's lien did not become choate until February 1972, when it was reduced to judgment in the state court.

ARGUMENT

I. THE DOCTRINES DEVELOPED BY THIS COURT TO DETERMINE LIEN PRIORITIES IN THE CONTEXTS OF THE INSOLVENCY STATUTE AND FEDERAL TAX LIENS ARE APPLICABLE IN THE CONTEXT OF FEDERAL CONTRACTUAL LIENS

A. This Court Has Framed Principles For Determining the Priority of Federal Liens in the Absence of Statutes Setting Priorities

The Small Business Administration (SBA) is authorized to make or guarantee loans to small-business concerns, provided that "the financial assistance applied for is not otherwise available on reasonable terms from non-Federal sources." 72 Stat. 387, as amended, 15 U.S.C. 636(a)(1). The SBA's loans must be "of such sound value or so secured as reasonably to assure repayment." 15 U.S.C. 636(a)(7). The priority of liens on real or personal property

acquired by the SBA to secure its loans is not established by federal statute, except in limited situations not presented here.[13] The relative priority of SBA liens is, however, clearly a question of federal law, as the court below recognized.[14] In these circumstances, "it is for the federal courts to fashion the governing rule of law according to their own standards." *Clearfield Trust Co.* v. *United States*, 318 U.S. 363, 367.

This Court has already fashioned a rule of priority for federal liens where no federal statute sets the priorities. It has done so in the context of federal tax liens. The priority rules for federal tax liens were derived by the Court from its cases construing the insolvency statute, 31 U.S.C. 191 (R.S. 3466). That statute, which has been in effect in essentially its present form since 1797, provides that "[w]henever any person indebted to the United States is insolvent, * * * the debts due to the United States shall be first satisfied." The statute serves a public policy of "secur[ing] an adequate revenue to sustain the public burthens and discharge the public debts,"

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[13] See 15 U.S.C. 646 and discussion *infra*, pp. 33-37.

[14] Pet. App. 13a and n.9. "When the United States disburses its funds or pays its debts, it is exercising a constitutional function or power." *Clearfield Trust Co.* v. *United States*, 318 U.S. 363, 366. The "titles or liens" created in the course of exercising these constitutional functions "present questions of federal law not controlled by the law of any State." *United States* v. *County of Allegheny*, 322 U.S. 174, 183. See also *United States* v. *Security Trust & Savings Bank*, 340 U.S. 47, 49; *United States* v. *Little Lake Misere Land Co.*, 412 U.S. 580; *United States* v. *Gish*, 559 F.2d 572 (C.A. 9), certiorari denied, April 24, 1978 (No. 77-1191).

and the priority it gives the government has been liberally construed to that end. *United States* v. *State Bank of North Carolina*, 6 Pet. 29, 35; *United States* v. *Moore*, 423 U.S. 77, 81-82.

The government's priority under the insolvency statute cannot attach to property that did not belong to the debtor on the date of insolvency—for example, because of a *bona fide* conveyance by the debtor before that date. *United States* v. *Knott*, 298 U.S. 544, 549; *Conard* v. *Atlantic Isurance Co.*, 1 Pet. 386. Consequently, in a series of cases stretching back to *Thelusson* v. *Smith*, 2 Wheat. 396, this Court has considered whether non-federal liens operated to divest the debtor of his property and thus to preclude the government's claim. In each case, the Court has held that the liens were not sufficiently specific and perfected on the relevant date. Liens that were not specific in amount;[15] that lacked a known lienor;[16] that did not attach to specific property;[17] that were not immediately enforceable without judicial proceedings or were not reduced to the actual possession

[15] *New York* v. *Maclay*, 288 U.S. 290, 292-294; *United States* v. *Texas*, 314 U.S. 480, 487; *United States* v. *Waddill, Holland & Flinn, Inc.*, 323 U.S. 353, 357-358.

[16] *United States* v. *Knott*, *supra*, 298 U.S. at 550-551.

[17] *United States* v. *Texas*, *supra*, 314 U.S. at 487; *United States* v. *Waddill, Holland & Flinn, Inc.*, *supra*, 323 U.S. at 358, 359-360; *Illinois* v. *Campbell*, 329 U.S. 362, 373-376.

of the lienor,[18] have all been held "inchoate" and thus incapable of ousting the priority claim of the United States under the insolvency statute.[19]

In 1950, this Court considered what the federal rule should be when a federal tax lien is competing for priority with a private or state lien, but the debtor is not insolvent. *United States* v. *Security Trust & Savings Bank*, 340 U.S. 47. At that time, no federal statute determined the priority of federal tax liens.[20] The Court concluded that "a similar rule" to the one it had developed under the "kindred" insolvency statute must be applied:

> In cases involving a kindred matter, *i.e.*, the federal priority under R.S. § 3466, it has never

[18] *United States* v. *Gilbert Associates, Inc.*, 345 U.S. 361, 365-366; *United States* v. *Texas*, *supra*, 314 U.S. at 487-488.

[19] Because all these liens were held to be inchoate, the Court has never had to decide whether the priority given the United States by the insolvency statute can be overcome even by a prior lien that is specific and perfected. See *United States* v. *Gilbert Associates, Inc.*, *supra*, 345 U.S. at 365; *Illinois* v. *Campbell*, *supra*, 329 U.S. at 370 and cases cited; *United States* v. *Vermont*, 377 U.S. 351, 358 n.8.

[20] 26 U.S.C. (1952 ed.) 3672, 53 Stat. 449, did provide that the federal tax lien was not valid against certain categories of lienors—mortgagees, pledgees, purchasers, and judgment creditors—until notice of the tax lien was filed in the office specified by state law. See *United States* v. *Security Trust & Savings Bank*, *supra*, 340 U.S. at 51. This statute established the time when the federal lien attached, but did not govern the competition between a federal tax lien that had attached and rival liens.

In the 1966 Federal Tax Lien Act, 80 Stat. 1125, 26 U.S.C. 6323(a), Congress has now provided some specific priorities governing federal tax liens. See pp. 28-32, *infra*.

been held sufficient to defeat the federal priority merely to show a lien effective to protect the lienor against others than the Government, but contingent upon taking subsequent steps for enforcing it. *Illinois* v. *Campbell*, [329 U.S. at 374]. If the purpose of the federal tax lien statute to insure prompt and certain collection of taxes due the United States from tax delinquents is to be fulfilled, a similar rule must prevail here. [340 U.S. at 51; footnote omitted.]

The Court accordingly held in *Security Trust* that a subsequent federal tax lien was superior to a prior but "inchoate" attachment lien, even though state law accorded the attachment lien superiority over later-arising interests. 340 U.S. at 48-51.

In succeeding cases, this Court held that the priority of federal tax liens was determined by the rule, "widely accepted and applied, in the absence of legislation to the contrary," that "'the first in time is the first in right.'" *United States* v. *City of New Britain*, 347 U.S. 81, 85.[21] And the Court reaffirmed the rule of *Security Trust* that "a competing lien must be choate in order to take priority over a later federal tax lien * * *." *United States* v. *Vermont*, 377 U.S. 351, 355; *United States* v. *City of New Britain*, *supra*, 347 U.S. at 86.

The Court also specified the criteria for determining when a non-federal lien is sufficiently specific and

[21] The Court concluded "that Congress had this cardinal rule in mind when it enacted [the statute creating the federal tax lien], a schedule of priority not being set forth therein." 347 U.S. at 86.

perfected, or "choate," to compete with the federal tax lien for first in time. In brief, this is so "when the identity of the lienor, the property subject to the lien, and the amount of the lien are established." *United States* v. *City of New Britain*, *supra*, 347 U.S. at 84; *United States* v. *Vermont*, *supra*, 377 U.S. at 358.

B. The Reasons Recognized by This Court for Applying the "First in Time" and "Choateness" Rules to Federal Tax Liens Are Equally Applicable to Federal Contractual Liens

In dealing with federal tax liens this Court has fashioned a federal rule, derived from the case law under the insolvency statute, that determines priorities on the basis of the "first in time" rule and the requirement that a non-federal lien be "choate" in order to compete for first in time. The reasons that led the Court to apply these doctrines to federal tax liens are equally applicable to federal contractual liens, including the SBA lien at issue in this case.

1. This Court applied the choateness requirement and the first-in-time rule to federal tax liens because it considered those rules necessary "to insure prompt and certain collection of taxes due the United States from tax delinquents * * *." *United States* v. *Security Trust & Savings Bank*, *supra*, 340 U.S. at 51. This purpose was nowhere explicit in the statute creating the federal tax lien, but the Court, invoking the analogy of the federal priority under the insolvency statute, had no difficulty in discerning it.

The choateness doctrine and the first-in-time rule are no less necessary to insure the collection of debts arising from federal loans and guarantees. The insolvency statute, under which the Court developed the choateness doctrine, makes no distinction between tax and contractual revenues. It applies to all situations in which the government is a creditor and the debtor an "insolvent"—situations involving contractual debts as well as tax debts. See *Price* v. *United States*, 269 U.S. 492, 501.[22] This is not surprising, since it is difficult to identify a material distinction between a dollar received from the collection of taxes and a dollar returned to the Treasury on repayment of a federal loan. Both are equally useful "to sustain the public burthens and discharge the public debts."

[22] The insolvency statute (R.S. 3466)—which "is almost as old as the Constitution, and its roots reach back even further into the English common law," *United States* v. *Moore*, *supra*, 423 U.S. at 80—thus stands against the suggestion of the court below (Pet. App. 18a-19a) that the collection of contractual debts owed the SBA and other federal agencies as a result of their programs is "less central to the proper functioning of the national government" than the collection of tax revenues. Here, as in its earlier statement that "[t]he collection of taxes is certainly more vital to the government's existence than the making of farm loans," *Connecticut Mutual Life Ins. Co.* v. *Carter*, 446 F.2d 136, 139, the Fifth Circuit is, at bottom, confusing the government's collection of revenues with its use of the collected revenues in governmental functions. Revenues are not collected to support "the government's existence" in the abstract, but to enable the performance of governmental services and functions; these include the making of loans by government lending agencies such as the Small Business Administration.

United States v. *State Bank of North Carolina*, *supra*, 6 Pet. at 35.

In the case of the Small Business Administration, Congress has left no doubt that, within the limits dictated by the remedial purposes of the statute, it wants the sums lent by the agency returned to the Treasury on termination of the loans. Congress required specifically that all loans made by the SBA be of "sound value or so secured as reasonably to assure repayment." 15 U.S.C. 636(a)(7). The repayment of loans and recovery of security interests are particularly important to the SBA's program, because amounts recovered are returned to a revolving fund in the Treasury that must serve as the source of new loans and guarantees, except to the extent that Congress provides additional appropriations. 15 U.S.C. 633(c).[23]

2. This Court's adoption of the first-in-time rule and the choateness doctrine in the context of tax liens stemmed also from a recognition that the states are not free to defeat a vested federal property interest. To safeguard the integrity of the federal lien, interests of rival creditors in the debtor's property must be scrutinized to assure that they were

[23] Inability of the Small Business Administration to realize on the security for its loans would have a substantial impact on its program. As of June 1978, the SBA reports that its outstanding direct loans and guarantees amounted to $9.6 billion and that at most times approximately $1.1 billion was in default, arrears, or liquidation. (In that month there were 11,997 loans in liquidation, involving $617,800,000. An additional 27,462 loans were delinquent, involving $520,700,000.)

specific and perfected before the federal lien attached. As the Court said in *United States* v. *City of New Britain*, *supra*, the choateness doctrine is necessary because "[o]therwise, a State could affect the standing of federal liens, contrary to established doctrine, simply by causing an inchoate lien to attach at some arbitrary time even before the amount of the tax, assessment, etc., is determined." 347 U.S. at 86 (footnote omitted).[24]

To undercut federal property rights is to interfere with the constitutional functions of the federal government that give rise to those rights.[25] In the case of tax liens, "to give priority to an inchoate state lien perfected after the federal lien for taxes has arisen is an interference with the federal power to lay and collect taxes." Sarner, p. 24, n. 24, *supra*, 95 U.Pa. L. Rev. at 758.[26] The constitutional functions of the federal government are no less implicated in federal contractual liens that arise in the course of federal lending programs, such as the lien of the Small Business Administration at issue here.[27] Just as this Court applied the choateness requirement in the tax lien context to prevent a state from undercutting "the standing of federal liens * * *" (*United States* v. *City of New Britain*, *supra*, 347 U.S. at 86), the same need to protect federal property and federal programs requires adherence to that requirement here. Like a federal tax lien, the SBA lien is a federal property interest that cannot be impaired or superseded by later-attaching interests to which state law purports to give priority,[28] unless Congress so provides.

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[24] As the Court's statement suggests, some form of a choateness requirement is a necessary complement to the first-in-time rule. Otherwise, "by the mere *ipse dixit* in the state statute creating a lien date, the lien of the United States is lost even though everything necessary to be done to establish the state lien takes place after [the federal lien] has arisen." Sarner, *Correlation of Priority and Lien Rights in the Collection of Federal Taxes*, 95 U. Pa. L. Rev. 739, 758 (1947) (cited with approval in *United States* v. *City of New Britain*, *supra*, 347 U.S. at 86 n.9).

[25] Such interference is, of course, beyond a state's power. See, *e.g.*, *McCulloch* v. *Maryland*, 4 Wheat. 316, 436 (state tax on national bank); *City of New Brunswick* v. *United States*, 276 U.S. 547 (state tax lien on federal mortgage); *United States* v. *Ansonia Brass & Copper Co.*, 218 U.S. 452, 470-471 (private lien on vessel owned by United States).

[26] "Hence it is not debatable that a tax lien imposed by a law of Congress, as we have held the present lien is imposed, cannot, without the consent of Congress, be displaced by later liens imposed by authority of any state law or judicial decision." *Michigan* v. *United States*, 317 U.S. 338, 340.

[27] *Cf. United States* v. *Roessling*, 280 F.2d 933, 936 (C.A. 5, 1960) (federal mortgage lien):

> No state or county can tax the property interests of the United States in the absence of congressional consent. There is no constitutional prohibition against a state or county assessing taxes against property on which the United States holds a lien on the basis of the full value of that property, but, in the absence of congressional consent, the state or county is without authority to enforce the collection of the taxes thus assessed so as to destroy the pre-existing federal lien. [Citations omitted.]

[28] This is true whether the state law purports to create the priority by way of relation-back or otherwise. With respect to state liens competing with federal tax liens, the Court has refused to apply "the long since rejected relation-back doctrine." *United States* v. *Pioneer American Insurance Co.*,

C. The Federal Tax Lien Act of 1966 Applies Only to Tax Liens And Provides No Basis for Abandoning the Clear And Until-Then Unanimous Federal Jurisprudence Concerning the Priority of Federal Non-Tax Liens

Following this Court's 1950 decision in *United States* v. *Security Trust & Savings Bank*, 340 U.S. 47, see pp. 19-20, *supra*, the lower federal courts proceeded to consider whether the rules applied there in determining the priority of federal tax liens were applicable to non-tax liens as well. Prior to enactment of the Federal Tax Lien Act of 1966 (80 Stat. 1125, as amended, 26 U.S.C. 6323), five courts of appeals considered the question, and all of them answered yes. The Third, Fifth, Seventh, Eighth, and Tenth Circuits agreed that the rules of first-in-time and choateness were no less applicable to federal contractual liens than they were to federal tax liens. *United States* v. *Oswald and Hess Co.*, 345 F.2d 886 (C.A. 3, 1965); *United States* v. *Roessling*, 280 F.2d 933 (C.A. 5, 1960); *United States* v. *County of Iowa*, 295 F.2d 257 (C.A. 7, 1961); *United States* v. *Latrobe Construction Co.*, 246 F.2d 357 (C.A. 8, 1957), certiorari denied, 355 U.S. 890; *Southwest Engine Co.* v. *United States*, 275 F.2d 106 (C.A. 10, 1960).[29]

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374 U.S. 84, 92 n. 11. See also *United States* v. *Security Trust & Savings Bank, supra*, 340 U.S. at 50.

[29] It was "settled law that prior to the Federal Tax Lien Act of 1966, both federal tax liens and federal mortgage liens took priority over all competing liens except those which became 'choate' before the federal lien attached." *Connecticut Mutual Life Insurance Co.* v. *Carter*, 446 F.2d 136, 141 (C.A. 5, 1971), certiorari denied, 404 U.S. 857 (Rives, J., dissenting; footnotes omitted).

Since enactment of the Federal Tax Lien Act of 1966, the courts of appeals for the First, Second, Seventh, and Tenth Circuits have reached the same conclusion, rejecting the argument that the Tax Lien Act has any bearing on the priority of federal non-tax liens. *Chicago Title Insurance Co.* v. *Sherred Village Associates*, 568 F.2d 217 (C.A. 1, 1978), petition for certiorari pending *sub nom. Hercoform Incorporated* v. *Chicago Title Insurance Company* (No. 77-1611); *United States* v. *General Douglas MacArthur Senior Village, Inc.*, 470 F.2d 675 (C.A. 2, 1972), certiorari denied *sub nom. County of Nassau* v. *United States*, 412 U.S. 922; *Willow Creek Lumber Co., Inc.* v. *Porter County Plumbing & Heating, Inc.*, 572 F.2d 588 (C.A. 7, 1978); *T. H. Rogers Lumber Co.* v. *Apel*, 468 F.2d 14 (C.A. 10, 1972).[30] And the Fourth Circuit and the Court of Claims, in cases involving federal claims other than liens, have likewise rejected the argument that the effect of the Tax Lien Act goes beyond tax liens. *H. B. Agsten & Sons, Inc.* v. *Huntington Trust & Savings Bank*, 388 F.2d 156, 160 (C.A. 4, 1967) (*en banc*), certiorari denied, 390 U.S. 1025; *Aetna Insurance Co.* v. *United States*, 456 F.2d 773, 776-777 (Ct. Cl., 1972).

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[30] The two most recent of these decisions expressly decline to follow the decision of the court of appeals in this case. *Willow Creek Lumber Co., supra*, 572 F.2d at 590-591; *Chicago Title Insurance Co., supra*, 568 F.2d at 222.

However, two courts of appeals, the court below (Pet. App. 20a-23a)[31] and the Ninth Circuit,[32] have concluded that the Federal Tax Lien Act of 1966, which modified the choateness doctrine as applied to tax liens, requires the federal courts to abandon that doctrine as applied to federal non-tax liens.

In so concluding, the court below and the Ninth Circuit have misinterpreted Congress's intent. In addition, they have invoked "policy reasons" that are inadequate and have proposed new rules that would inject needless uncertainty and complexity into commercial affairs (see pp. 37-51, *infra*).

1. The court below reasoned that, in view of the Federal Tax Lien Act of 1966, "logical symmetry urges rejection of the SBA's efforts to extend the choateness doctrine" to SBA liens (Pet. App. 20a), and that "the Act's recognition that some state claims should have priority over federal tax liens is a strong policy argument against extending the choateness doctrine to deny priority to state claims" (Pet. App. 21a, n.12).[33] This reasoning purports to find in the

[31] See also *United States* v. *Crittenden*, 563 F.2d 678 (C.A. 5, 1977), petition for certiorari pending (No. 77-1644); *Connecticut Mutual Life Insurance Co.* v. *Carter*, 446 F.2d 136 (C.A. 5, 1971), certiorari denied, 404 U.S. 857.

[32] See *United States* v. *California-Oregon Plywood, Inc.*, 527 F.2d 687 (C.A. 9, 1975); *Ault* v. *United States* 432 F.2d 441 (C.A. 9, 1970), affirming *Ault* v. *Harris*, 317 F. Supp. 373 (D. Alaska).

[33] Similar reasoning was earlier relied on by the Fifth Circuit in *Connecticut Mutual Life Ins. Co.* v. *Carter, supra*, 446 F.2d at 139, and by the Ninth Circuit in *Ault* v. *Harris, supra*, 317 F. Supp. at 375-376, affirmed and opinion adopted, *Ault*

Tax Lien Act congressional guidance extending beyond the area of tax liens. No such guidance is there.

The Federal Tax Lien Act of 1966 (80 Stat. 1125) amended 26 U.S.C. 6323 by broadening the protection given creditors who have liens competing with the federal tax lien imposed by 26 U.S.C. 6321. Among other things, the Act added mechanics' liens to the class of liens protected against tax liens of which notice has not been filed (26 U.S.C. 6323(a)); added certain categories of liens to those given a "superpriority" effective even against a tax lien of which notice has been filed (26 U.S.C. 6323(b)); and provided priority for interests arising subsequent to the filing of notice of the tax lien if those interests are protected by local law and if they arise from specified types of financing agreements that cover the property in question and that were entered into before the filing of notice of the tax lien (26 U.S.C. 6323(c)).

The Act thus provides only limited exceptions to the choateness rule in the context of federal tax liens.[34] The House Report, after reciting the require-

v. *United States, supra*, 432 F.2d 441, and *United States* v. *California-Oregon Plywood, Inc., supra*, 527 F.2d at 689.

[34] For example, the Act does not protect mechanics' liens that arise before the lienors provide services or materials, even if these would be protected under state law against later-arising liens. 26 U.S.C. 6323(h)(2); Plumb, *Federal Tax Liens* 152 (3d ed. 1972). And the Act gives priority to future advances pursuant to a written commercial financing agreement only if they are made within 45 days of the filing of the tax lien and without notice of that filing. 26 U.S.C. 6323(c)(2)(A).

ments of that rule as established by this Court in *United States* v. *City of New Britain*, *supra*, noted that "[e]xcept as otherwise provided, subsection (a) of [the Act] retains this basic rule of Federal law." H.R. Rep. No. 1884, 89th Cong., 2d Sess. 35 (1966).[35]

The Act was concerned, as its title indicates and as both of the congressional committee reports confirm, only with federal tax liens. It was a "comprehensive revision and modernization of the provisions of the internal revenue laws concerned with the relationship of Federal tax liens to the interests of other creditors." S. Rep. No. 1708, 89th Cong., 2d Sess. 1 (1966); H.R. Rep. No. 1884, *supra*, at 1. Nothing in the text of the Act, the committee reports, or the debates suggests a congressional intention to provide guidance of any sort concerning the relative priorities of federal liens other than tax liens. See H.R. Rep. No. 1884, *supra*, *passim*; S. Rep. No. 1708, *supra*, *passim*; 112 Cong. Rec. 22209-22211, 22224-22235, 26476-26478, 28218-28219 (1966).[36]

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[35] The court below recognized that the Act did not abolish the choateness doctrine with respect to tax liens, but only "adjusted the application of the doctrine by recognizing the priority of certain state interests, essentially granting exceptions to the choateness doctrine" (Pet. App. 20a-21a, n.12). Thus, a court could achieve "logical symmetry" only by adopting the rules of the Tax Lien Act for use in all non-tax lien cases, not by abolishing the choateness doctrine and casting about for new rules of the court's own devising.

[36] Representative Mills, Chairman of the Committee on Ways and Means, in response to questioning, specifically disavowed any intention to affect bankruptcy priorities. 112 Cong. Rec. 22226 (1966).

The Act was based on a draft prepared by the American Bar Association's Special Committee on Federal Liens. A member of that committee has written:

> The mandate of the American Bar Association's Special Committee on Federal Liens was, as its name indicates, not limited to *tax* liens. Nevertheless, because of limitations of time and personnel, and the practical desirability of focusing its negotiations on one government department and one committee in each branch of Congress, the Special Committee's final proposals, and to a greater extent the legislation which evolved, dealt primarily with the tax situation, leaving to another day the extension of the reforms to other areas.

Plumb, *Federal Liens and Priorities—Agenda for the Next Decade*, 77 Yale L.J. 228, 285 (1967) (emphasis in original; footnotes omitted); see also 83 Reports of the American Bar Association 453 (1958); 84 Reports of the American Bar Association 645, 671-672 (1959).

The content and background of the Federal Tax Lien Act thus permit only one inference about the asserted impact of that Act on the previously established law concerning the priorities of federal non-tax liens. This is the inference drawn by the Second Circuit—in agreement with four other courts of appeals and the Court of Claims [37]—as follows:

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[37] See p. 27, *supra*. "We conclude from the foregoing discussion of the legislative history that Congress intended

> We are unable to conclude * * * that a Congressional enactment, carefully drawn, which affects the priority of federal *tax* liens leaves the courts free to disregard prior precedents and thus to broadly extend the scope of the statute's principle to other unspecified areas which, though somewhat analogous, were simply not addressed by the Congress.

United States v. *General Douglas MacArthur Senior Village, Inc.*, 470 F.2d 675, 678-679 (C.A. 2), certiorari denied *sub nom. County of Nassau* v. *United States*, 412 U.S. 922 (emphasis in original).[38]

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in the Federal Tax Lien Act of 1966 to legislate only with respect to the priority accorded the Federal tax lien * * *." *Aetna Insurance Co.* v. *United States, supra*, 456 F.2d at 776-777.

[38] If Congress had considered the question, there are plenty of reasons why it might have decided that federal tax liens and non-tax liens should not be treated the same way. For example: "We cannot say that it is illogical for Congress to deem it desirable to retain a priority for money it loans, while relinquishing the priority for its tax liens, which represent no financial outlay. Whatever may be the merits of symmetry in these two quite distinct, if cognate, areas the argument seems more properly addressed to Congress than to this court." *H. B. Agsten & Sons, Inc.* v. *Huntington Trust & Savings Bank, supra*, 388 F.2d 156, 160 (C.A. 4, 1967) (Sobeloff, J.). "Government taxes are so certain that the President is recommending to the Congress that the Government share its revenues with the States and municipalities. It is not irrational for Congress to think that the Government can afford to relax in favor of private liens the protection heretofore afforded liens for taxes, but that the strict protection should remain in force as applied to the limited and specific appropriations made by Congress to federal lending agencies." *Connecticut Mutual Life Insurance Company* v. *Carter, supra*, 446 F.2d 136, 143 (Rives, J., dissenting).

2. Moreover, Congress in another enactment has dealt specifically with the priority of liens of the Small Business Administration and has limited that priority in only a particular way. This statute, 15 U.S.C. 646, enacted in 1958 (72 Stat. 396) as an amendment to the Small Business Act, expressly subordinates SBA liens to state and local liens for property taxes.[39]

The legislative history of 15 U.S.C. 646 supports the inference that Congress intended only this limited exception to the priority that SBA liens could otherwise claim by virtue of judicial decisions. The legislation was originally introduced by Senator Payne, with the purpose of establishing that "all tax liens * * * will take priority over SBA mortgage claims." 104 Cong. Rec. 2470 (1958). What Senator Payne's bill provided, however, was that "any debt due the Administration * * * shall not be entitled to

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[39] 15 U.S.C. 646 provides:

> Any interest held by the Administration in property, as security for a loan, shall be subordinate to any lien on such property for taxes due on the property to a State, or political subdivision thereof, in any case where such lien would, under applicable State law, be superior to such interest if such interest were held by any party other than the United States.

The statute does not apply to state and local taxes that are not levied on real property. See, *e.g.*, *Director of Revenue, State of Colorado* v. *United States*, 392 F.2d 307, 312 (C.A. 10) (sales and withholding taxes not covered); *United States* v. *Oswald and Hess Co., supra*, 345 F.2d at 888 (water and sewer charges not covered). See p. 7, n. 9, *supra*.

the priority available to the United States pursuant to section 3466 of the Revised Statutes (31 U.S.C. 191) [the insolvency statute]." *Ibid.* The Small Business Administration, in commenting to the Senate Committee on the proposed legislation, stated that it supported Senator Payne's objective but did not believe that the bill, as drafted, accomplished its aims. Letter from Wendell B. Barnes, Administrator, Small Business Administration, in Hearings before a Subcommittee of the Senate Committee on Banking and Currency, Credit Needs of Small Business, 85th Cong., 2d Sess. 553-554 (1958) ("Hearings"). The SBA proposed alternative language, which, with minor modifications, was adopted by the Senate Committee and became 15 U.S.C. 646.

The SBA told the Senate Committee that Senator Payne's bill, as drafted, was both too broad and too narrow. It was too broad because it would deprive the SBA of its priority under the insolvency statute not only against state and local tax liens, but against all competing liens. The SBA opposed this aspect of the bill because "we often find it necessary to assert that priority against creditors other than State or local taxing authorities," and "[i]n this manner, we have recovered large amounts of money which would otherwise have been lost to the Government." Hearings, *supra*, at 553.

On the other hand, the bill was too narrow because it removed the SBA's priority against state and local tax liens only in the context of the insolvency statute. It thus "offer[ed] little of practical value to

local taxing authorities," since "the real conflict between their rights and ours lies in areas which are not affected by the priority contained in [the insolvency statute]." *Ibid.*

The SBA stated that "[u]ntil recently," it had avoided such conflicts "by yielding to the demands of local tax authorities," since "[n]ormally their claims are small in relation to the total amounts involved and, in such cases, we considered it to be in the best interests of the Government to avoid the expense and delay entailed in litigating the matter." *Ibid.* Also, there was doubt whether the rule established by this Court in *United States* v. *City of New Britain, supra*—that "as between a Federal tax lien and a State or local tax lien, the lien which attaches first in point of time is the superior"—was applicable to SBA mortgage liens. Hearings, *supra*, at 553.

But in January 1958, the SBA continued, the Court of Appeals for the Third Circuit had held in *United States* v. *Ringwood Iron Mines, Inc.*, 251 F.2d 145, "that a mortgage lien held by the United States stands in the same position as a tax lien held by the United States * * *." Hearings, *supra*, at 554. In view of that decision, the SBA had "reluctantly concluded that we have a duty to insist upon the superiority of our mortgages in all cases where they are prior, in point of time, to State or local tax liens." *Ibid.* The SBA therefore endorsed the proposed legislation, in the form suggested by the SBA (and ultimately enacted), "[i]n order to eliminate this situa-

tion" and permit the SBA to return to its practice of yielding to state and local tax liens. *Ibid.*

The issue presented by the Payne bill, together with the SBA's comments on it, thus focused Congress's attention on the priority of SBA contractual liens. In amending the bill as suggested by the SBA, the Congress was aware of, and apparently accepted, the SBA's opposition to a bill that would deprive it of priority against all competing creditors, so far as the insolvency statute was concerned, and would thus disable it from "recover[ing] large amounts of money which would otherwise * * * [be] lost to the Government." Hearings, *supra*, at 553. To be sure, the original Payne bill would have had this effect only with respect to the insolvency statute. But Congress hardly would have been more agreeable to the even greater loss of federal revenues that would result from depriving the SBA of priority against all competing creditors in the more common situations that are not governed by that statute.

What Congress enacted was the carefully limited bill, as proposed by the SBA, depriving SBA liens of priority against only a narrow class of competing security interests—liens held for property taxes by state and local governments. This enactment, dealing specifically and precisely with the priority of Small Business Administration liens, further refutes the claim that by the Federal Tax Lien Act of 1966, which dealt with nothing but tax liens, Congress intended to upset in wholesale fashion the priorities of

SBA liens in particular or federal contractual liens generally.[40]

D. In Abandoning the Choateness Rule, The Fifth Circuit Has Upset Established Law Without Good Reason And Has Substituted New Rules That Are Uncertain and Unreliable

Prior to the Federal Tax Lien Act of 1966, it was "settled law" [41]—the unanimous view of the five Circuits that considered the question [42]—that both federal tax liens and federal contractual liens took priority over all competing liens except those that had become "choate" before the federal lien attached. The court below has held that the Federal Tax Lien Act of 1966, *sub silentio* and without specifics, gave the courts a license to revamp this established law of non-tax liens. In so holding, the court has not only erred in its interpretation of the congressional intent (see pp. 28-31, *supra*). The Fifth Circuit is also

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[40] Also, the SBA's submission in 1958 put Congress on notice that, as a result of a court of appeals decision applying the rule of *United States* v. *City of New Britain* (347 U.S. 81) to federal mortgage liens, the SBA considered that "a mortgage lien held by the United States stands in the same position as a tax lien held by the United States * * *." Hearings, *supra*, at 553-554. Although the SBA's discussion did not mention the choateness doctrine specifically, that doctrine is at the heart of the Court's decision in *New Britain*. See 347 U.S. at 84, 86-87; pp. 20-21, *supra*. Moreover, as the Court there recognized, some form of a choateness rule is a necessary corollary of the first-in-time rule, which the SBA did mention. See 347 U.S. at 86; p. 24 and n. 24, *supra;* Hearings, *supra*, at 555.

[41] See note 29, *supra*.

[42] See p. 26, *supra*.

wrong because it has scuttled the previously settled doctrine in an area of law where certainty should prevail, because the asserted policy reasons for its action are unfounded, and because the *ad hoc* rules it proposes to substitute are ill-considered, ill-defined, and unreliable.

1. If "in most matters it is more important that the applicable rule of law be settled than that it be settled right," as long as "correction can be had by legislation" (*Burnet* v. *Coronado Oil & Gas Co.*, 285 U.S. 393, 406 (Brandeis, J., dissenting)), this is pre-eminently true in matters of commercial law. "Judicial decisions affecting the business interests of the country should not be disturbed except for the most cogent reasons, certainly not because of subsequent doubts as to their soundness. The prosperity of a commercial community depends, in a great degree, upon the stability of the rules by which its transactions are governed. If there should be a change, the legislature can make it with infinitely less derangement of those interests than would follow a new ruling of the court, for statutory regulations would operate only in the future." *National Bank* v. *Whitney*, 103 U.S. 99, 102.

Although it had not been determined directly by this Court, the law governing the relative priority of federal contractual liens—consisting of the first-in-time rule and the choateness doctrine—was firmly established in the courts of appeals prior to the 1966

Act.[43] The Court of Appeals for the Fifth Circuit should have followed that established law, since " 'presumably, individuals may have arranged their affairs in reliance on the expected stability of decision.' " *Monell* v. *Department of Social Services*, No. 75-1914, decided June 6, 1978, slip op. 39 (dictum) (quoting *Monroe* v. *Pape*, 365 U.S. 167, 221-222 (Frankfurter, J., dissenting)). In fact, in 1969, when the Small Business Administration entered into the loan guarantee whose priority is at issue here, the Fifth Circuit appeared to follow what was then the unanimous rule in the courts of appeals concerning the priority of federal contractual liens. *United States* v. *Roessling*, *supra*, 280 F.2d 933 (C.A. 5, 1960). The Fifth Circuit rejected the choateness doctrine only in June 1971 (*Connecticut Mutual Life Insurance Co.* v. *Carter*, *supra*, 446 F.2d 136, 138-139, certiorari denied, 404 U.S. 857).[44] This was after the SBA had guaranteed O.K.'s note, after O.K. had defaulted on the loan, and after the Bank had assigned its security interest to the SBA (see pp. 4-6, *supra*). The federal govern-

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[43] That law remains overwhelmingly recognized today. The Fifth and Ninth Circuits notwithstanding, the choateness doctrine and the first-in-time rule evidently govern in at least the First, Second, Third, Seventh, Eighth, and Tenth Circuits. See pp. 26-27, *supra*.

[44] The decision of the Ninth Circuit in *Ault* v. *United States*, 432 F.2d 441, see p. 28 n. 32, *supra*, was rendered in September 1970, also after the SBA entered into the loan guarantee here.

ment and other parties [45] stand to lose substantial sums, not only in this case but in hundreds of others, if their justified reliance on the choateness doctrine and the first-in-time rule proves to have been incorrect.

2. The Fifth Circuit's abandonment of the established rule might have been justified if the rule were clearly in error, a departure from prior practice, and not the subject of reliance. See *Monell* v. *Department of Social Services*, *supra*, slip op. 35-41. None of those conditions is true. The Fifth Circuit did not claim otherwise. Rather, viewing "the choateness doctrine independently," it decided that "strong policy reasons militate against its application in this context" (Pet. App. 17a; see also *id.* at 23a).

The court's belief that a new rule would reflect better policy was an insufficient basis for unsettling

[45] For example, in *Chicago Title Insurance Co.* v. *Sherred Village Associates*, 568 F.2d 217 (C.A. 1), the bank whose mortgage loan was insured by the Department of Housing and Urban Development had warranted to HUD, upon assignment of the mortgage loan to HUD, that the mortgage would have priority over all liens recorded after the date the mortgage was filed. Chicago Title Insurance Company, in turn, had insured the obligations of the bank under this warranty. See 568 F.2d at 219. If the choateness doctrine is not applicable, and state law applies instead, these warranties were incorrect; under Maine law, a mechanic's lien would take priority even though recorded after the mortgage, so long as the contract was signed before. See 568 F.2d at 218-219. The First Circuit decided to follow the choateness doctrine, and a petition for certiorari is pending (*sub nom. Hercoform Incorporated* v. *Chicago Title Insurance Company*, No. 77-1611).

the law in this area. But the court's policy arguments are in fact unfounded, and its effort to develop a new federal law of lien priorities on a case-by-case basis would produce results inferior to the rule it rejected.

The court's major policy justification for rejecting the choateness rule in favor of rules derived from state law and the Uniform Commercial Code appears to be its notion that the United States, through the Small Business Administration, acts as a "surrogate commercial lender," or a "quasi-commercial lender," and as such should get no better treatment than a private lender (Pet. App. 17a-18a).[46] The notion is erroneous. The Small Business Administration, like other government lending agencies, is decisively different from an ordinary commercial lender. Government loans, guarantees, and insurance are provided for reasons of national policy, not to make a profit. See the declaration of policy in the Small Business Act, 72 Stat. 384, 15 U.S.C. 631(a); *Federal Crop Insurance Corp.* v. *Merrill*, 332 U.S. 380, 383 and n. 1; see also *Indian Towing Co.* v. *United States*, 350 U.S. 61, 67-68. And they are provided, usually, only if commercial credit is not available on reasonable terms. See 15 U.S.C. 636(a)(1), quoted at p. 16, *supra;* see also, *e.g.*, 7 U.S.C. 1922(4), 1941(a)(4) (Farmers Home Administration); 42

[46] We have dealt earlier with the court's suggestion that revenues collected from loan repayments are "less central to the proper functioning of the national government" (Pet. App. 19a) then revenues collected from taxes. See p. 22 and n. 22, *supra*.

U.S.C. 3142(b)(4) (Economic Development Administration).[47]

The court of appeals was thus wrong in reasoning that the government should be treated as an ordinary commercial lender because it "enters the commercial credit scheme" with the same "opportunity to evaluate the credit risks" as a private lender (Pet. App. 18a). The government enters only where private lenders do not go. And the choateness rule provides appropriate protection for government loans where the government is the lender of last resort. See *Connecticut Mutual Life Insurance Company* v. *Carter*, *supra*, 446 F.2d at 142-143 (Rives, J., dissenting).[48]

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[47] SBA regulations require proof of refusal of the required financial assistance by the applicant's bank of account and, if the requested assistance is in excess of that bank's normal lending limit, by a correspondent bank as well; when a direct loan is sought, the regulations require proof of refusal by two financial institutions. 13 C.F.R. 120.2(a)(1). In addition, it must appear that the required financial assistance is not available through placement of securities, sale of excess assets, or use of personal credit. 13 C.F.R. 120.2(a)(2).

[48] The Fifth Circuit has characterized the first-in-time and choateness doctrines as a rule that "the government always wins." *United States* v. *Crittenden*, *supra*, 563 F.2d at 688. That is not the case. See *United States* v. *City of New Britain*, *supra*, 347 U.S. at 84, 88 (Court noted that certain tax and water-rent liens were apparently choate, and remanded for determination of priorities); *United States* v. *Vermont*, *supra*, 377 U.S. at 358-359 (tax lien held choate, because summarily enforceable); *Crest Finance Co.* v. *United States*, 368 U.S. 347 (lien held choate where the property to which it attached (accounts receivable), the amount due (face value of note), and the identity of the lienor were all certain). In *United States* v. *Vermont*, *supra*, the Court made it clear that the "absolute priority" (377 U.S. at 358) given the United States under the insolvency statute does not apply to lien contests outside that statute, and rejected the claim that "different standards of choateness apply to federal and state liens" (*id.* at 355).

Nor is there substance in the theory advanced by the court of appeals that the choateness doctrine harms small businesses, contrary to the congressional policy embodied in the Small Business Act, because it ~~lands~~ deters private creditors to shun businesses that might be eligible for SBA loans (Pet. App. 19a). This Court has rejected similar arguments in cases involving R.S. 3466, the insolvency statute. *Small Business Administration* v. *McClellan*, 364 U.S. 446, 453; see also *United States* v. *Remund*, 330 U.S. 539, 544; *United States* v. *Emory*, 314 U.S. 423, 431.[49] In fact, when the federal assistance improves the situation of the borrower, it normally helps the borrower's commercial creditors as well—making them more, not less, willing to lend additional sums. In the present case, for example, the SBA guarantee of the loan from the Bank in February 1969 enabled O.K. to retire outstanding indebtedness, including the $24,893.10 that it owed Kimbell on the April 1968 note, and to pay the amounts it owed Kimbell on

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[49] If the theory were valid, the commercial ostracism that the court posits presumably would have manifested itself in the jurisdictions that follow the choateness rule. The Small Business Administration informs us that its operations in those jurisdictions have encountered no such manifestations. Nor are we aware of any evidence from any other source that supports the court's conjecture.

open account (see p. 5, *supra*). The guarantee also provided needed operating funds for O.K.'s troubled business, all to the benefit of O.K.'s creditors, including Kimbell, which continued to advance credit to O.K.[50]

Even if the established priority rules did cause some commercial lenders to treat loans to small businesses as somewhat riskier than otherwise, an alteration in the priority rules could not be assumed to produce a net benefit for small businesses. The Small Business Administration, like other federal lending or insuring agencies, has only limited resources. It uses a revolving fund as the source of loans and guarantees (15 U.S.C. 633(c)). Inability of the SBA to realize on the security for its loans simply reduces the amount available for future loans, to the detriment of small businesses.

3. The federal rules of lien priority developed by this Court in connection with federal tax liens, and applied by the overwhelming majority of the courts of appeals in connection with federal non-tax liens, form a coherent, well-established, well-understood body of precedent. This law can be readily applied by the courts. And it can be readily utilized in the commercial world to determine in advance the relative rights of the parties to commercial transactions, and to shape the transactions accordingly. The same cannot be said of the new priority rules that the court

[50] The Small Business Administration can, and does, subordinate its liens *by contract* to the claims of other creditors when this is necessary or appropriate. The choateness rule thus provides the SBA with an operational flexibility that the rule of the court below would remove.

below has set out to develop. The court's approach would proceed on a case-by-case basis, selecting from a variety of sources of law, and would produce results virtually impossible to predict and rely on. This judicial regime would be far from conducive to "the expected stability of decision" (*Monell* v. *Department of Social Sciences*, *supra*, slip op. 39).

Thus, once it had discarded the choateness rule, the court in the present case was faced with two difficult issues—"how does a federal court determine when a state lien has arisen so that it may decide whether the state or the federal lien is 'first in time' " (Pet. App. 24a), and whether, under the federal common law that the court was creating, Kimbell's lien for future advances related back to the date of the original security agreement (Pet. App. 26a).[51] On the first question, the court determined that, "[w]hatever the answer * * * may be in other contexts"—which "present problems that we leave for another day" (Pet. App. 24a-25a and n. 15)—here the answer was to look to the Uniform Commercial Code (Pet. App. 24a-25a). Yet, on the second question the court refused to commit itself to the

[51] The court conceded that, having abandoned the choateness doctrine, it was left at large in dealing with this issue:

> Perhaps because of the pervasiveness of the choateness doctrine, we have found no federal case discussing the substantive content of the "first in time, first in right" rule with regard to future advances. Faced with the necessity of fashioning a federal common-law rule because of congressional silence on the subject, we grapple with the problem by first examining the approach taken by the states. [Pet. App. 26a; citations omitted.]

U.C.C. rule, and "grapple[d] with the problem by first examining the approach taken by the states" (Pet. App. 26a-27a). The court identified three rules that had been applied by state courts and narrowed its choice to two, finding it unnecessary to decide between them in this case and leaving "final resolution of this difficult decision for another day" (Pet. App. 26a-28a and n. 18).

The court's mode of decision-making illustrates well the uncertainties arising from any attempt to develop new priority rules through litigation. As the Court of Appeals for the First Circuit said in *Chicago Title Insurance Co.* v. *Sherred Village Associates*, *supra*, in the course of rejecting the approach of the Fifth Circuit here: "We cannot avoid feeling that there is much that we do not know about the equities, effects of various rules, and relative ability of the federal and local lienors to protect themselves," and new rules "could be more equitably and intelligently made after Congressional hearings, rather than after a trial between a limited number of litigants" (568 F.2d at 221 and n. 6).[52]

[52] The Fifth Circuit's decision in *United States* v. *Crittenden*, *supra*, provides a further example of the number of legal issues that can be raised in determining lien priorities, the variety of possible rules that can be applied to each issue, and the difficulty of predicting what rule the court will choose. In *Crittenden*, the court (1) chose the model U.C.C. over state law in fashioning a general rule of priority for mechanics' liens (563 F.2d at 688-689); (2) then followed the model U.C.C. in looking to state law to determine whether a lien had been created (noting that in some circumstances it would follow neither the model U.C.C. nor state law) (*id.* at 690 and n. 20); and (3) finally considered both the U.C.C. case law and the rule of the Federal Tax Lien Act of 1966, and chose the latter, on the question whether the mechanic must have maintained continuous possession of the property subject to the lien (*id.* at 691). The court's ultimate result appears to have given the private lienor a priority under federal law that he would have been denied under state law (see *id.* at 688-689 and n. 17), a result that probably surprised him as much as it did the United States.

4. In addition to shattering "the expected stability of decision," the court below has not justified even the general tendency of the choice of rules it finally arrived at. That tendency favors rules drawn from state law or the model U.C.C.[53] The soundness of this choice is open to question.

One approach considered by the American Bar Association's Special Committee on Tax Liens, in framing the proposed legislation that became the Federal Tax Lien Act of 1966, was to adopt state law as the federal rule—"to put the federal tax lien on the same basis under state law as competing liens." 84 Reports of the American Bar Association 647 (1958). The Committe rejected this approach (*id.* at 648). It did so in response to criticism that "state priority laws were adopted with reference to the competing interests of private claimants, without the federal government in mind—and that, in many cases, the several states exempted themselves from the very

[53] The Ninth Circuit likewise appears to favor state law, although its cases can also be read as adopting the Federal Tax Lien Act of 1966, which, with respect to the facts presented, would have followed state law. See *United States* v. *California-Oregon Plywood, Inc.*, *supra*, 527 F.2d at 689, 691; *Ault* v. *Harris*, *supra*, 317 F. Supp. at 375-376, affirmed and opinion adopted, *Ault* v. *United States*, 432 F.2d 441.

priorities which it is sometimes urged should be applied against the United States" (*ibid.*). The opponents of the state law approach further argued that "the merits of each type of case should be weighed to determine whether it ought to be the federal government or the competing lienor who should have priority," and that "Congress should make the policy decision as to where the federal tax lien should rank in relation to various other categories of competing lien interests" (84 Reports of the American Bar Association at 648).

Instead of the state law approach, the Committee adopted a "selective federal" approach (*id.* at 648). Under this recommendation no person would be granted any lien or other claim that he did not possess under state law, and "federal law would set limits (in each instance tailored to the circumstances of particular types of liens) beyond which such lien would not be recognized as against the federal tax lien" (*ibid.*). This "selective federal" approach was ultimately adopted in the Federal Tax Lien Act of 1966. See, *e.g.*, H.R. Rep. No. 1884, *supra*, at 1-3.

The objections to the state law approach that were made in the context of the tax lien legislation apply equally to the Fifth Circuit's affinity for state law in the context of non-tax liens. State laws on lien priorities were not adopted with federal interests in mind. They may exempt the states themselves from priorities they would apply against the United States.[54] And they do not allow for weighing the

[54] See, *e.g.*, Cal. Revenue and Taxation Code § 2192.1 (West 1978 Supp.); Fla. Stat. § 197.056 (1978); Ohio Rev. Code

federal claim on its merits against the claim of the competing state or private lienor in the contexts of the various categories of liens.

With or without deference to state law, the federal courts are not well-suited to make decisions of this kind. See *Chicago Title Insurance Co.* v. *Sherred Village Associates*, quoted at p. 46, *supra*, 568 F.2d at 221 and n. 6; see also *id.* at 222. As the Court of Appeals for the Second Circuit has said, "* * * the soundest approach would be to look to Congress for resolution rather than to the judiciary," since "Congress has the fact gathering facilities so necessary for an appropriate gauging of the impact of a decision to waive the federal priority for mortgage liens, and Congress is best-suited to make the necessary judgment whether to return a portion of federal revenues to local governments [in the case of competing state and local tax liens]." *United States* v. *General Douglas MacArthur Senior Village, Inc.*, *supra*, 470 F.2d at 679.

The result of congressional consideration would be, probably, a uniform federal rule.[55] In any event, any

§ 715.261 (1976); *Cleveland Metropolitan Housing Authority* v. *Lincoln Property Management Co., Inc.*, 22 Ohio App. 2d 157, 259 N.E.2d 512; 72 Penn. Stat. Ann. § 1401 (1978 Supp.).

[55] Such a rule is established for tax liens by the Federal Tax Lien Act of 1966. If the Fifth Circuit had adopted that Act as the model for a new rule governing federal non-tax liens, it would at least have produced a rule that facilitated the prediction of judicial results and provided some uniformity of treatment for liens arising from loans made in different states under the same federal program. However, we do not believe

congressional decision to incorporate state law would be made only after due consideration of the adverse impact on federal revenues, as well as the adverse effects that the resulting lack of uniformity would have on the administration of federal programs. See *Clearfield Trust Co.* v. *United States*, 318 U.S. 363, 367; *D'Oench, Duhme & Co.* v. *Federal Deposit Insurance Corp.*, 315 U.S. 447, 471-473 (Jackson, J., concurring).[56] Leaving to Congress the decision

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that such a decision would have been appropriate. The federal interests protected by the first-in-time and choateness rules—such as assuring the repayment of loans to federal programs and preventing the states from undercutting federal property interests (see pp. 21-25, *supra*)—should not be waived except by Act of Congress; Congress is the appropriate body to determine whether to relinquish federal revenues in the asserted interest of fairness to competing lienors. No such Congressional action or intent can be inferred, with respect to the issues here, from either the Federal Tax Lien Act of 1966 or the 1958 amendment to the Small Business Act, 15 U.S.C. 646 (see pp. 26-27, *supra*). Moreover, there is no reason to assume that Congress would apply to federal non-tax liens the same policies—let alone the same specific provisions with respect to the various categories of federal liens and competing liens—that it applied to tax liens in the 1966 Act (see p. 32, n. 38, *supra*). Finally, whether or not a new judicial rule would be modeled on a legislative enactment, the need for certainty in commercial law is better promoted when changes in the law are made by actual legislation than when they are made by judicial decision. See *National Bank* v. *Whitney*, *supra*, 103 U.S. at 102.

[56] Recognizing the interest in uniformity, the Fifth Circuit has justified its reliance on the Uniform Commercial Code as a source of federal law by asserting that "the UCC embodies rules of nationwide applicability—all states but Louisiana have adopted it—assuring that federal contractual liens will

whether to modify or even eliminate the first-in-time and choateness rules with respect to federal contractual liens, and the determination of what the new rules should be for the various kinds of federal liens and various kinds of competing liens, would preserve in this area of commercial law both the stability and the uniformity of decision that are threatened by the approach of the court below.

II. RESPONDENT'S LIEN FOR FUTURE ADVANCES WAS INCHOATE AT THE TIME THE FEDERAL LIEN ATTACHED AND THEREFORE IS JUNIOR

For the reasons set forth in Part I, *supra*, we submit that the first-in-time and choateness rules should be applied to determine the priority of federal contractual liens and, in particular, of the Small Business Administration lien in this case.[57] Under

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not be subject to the idiosyncrasies of particular state laws." Pet. App. 25a; see also *United States* v. *Crittenden*, *supra*, 563 F.2d at 689-690. The court overestimates the uniformity that would result from application of the U.C.C. A number of states have amended the model U.C.C. in adopting it, and state court constructions of it vary. The alternative of applying the model U.C.C. provisions, instead of the actual law of the particular state (see *United States* v. *Crittenden*, *supra*, 563 F.2d at 688-689), would not seem conducive to the certainty of commercial affairs within that State. In addition, as the court below recognized (Pet. App. 24a and n. 15), a wide variety of liens, including mechanics' liens and state and local tax liens, are not provided for by the U.C.C.

[57] This general statement is, of course, subject to the exception that a federal statute may provide otherwise, as 15 U.S.C. 646 does with respect to SBA liens competing with state or local property-tax liens (see pp. 33-37, *supra*)—an issue not presented by this case (see note 9, *supra*).

those rules, respondent Kimbell's lien for future advances did not become choate until after the SBA lien had attached, and the SBA lien is therefore first in time and entitled to priority in the proceeds being held in escrow by the Republic National Bank of Dallas.

A. The court of appeals was correct in ruling (Pet. App. 26a) that the SBA's security interest in the property of O.K. Super Markets attached when the Republic National Bank's security agreement was filed, in February 1969. See *United States* v. *Eklund*, 369 F. Supp. 1052, 1054-1055 (S.D. Ill. 1972); cf. *Small Business Administration* v. *McClellan*, *supra*, 364 U.S. at 450. At that time the government's obligation to guarantee 90 percent of the Bank's loan pursuant to its agreement with the Bank—and to pay the Bank 90 percent of the loan in the event of default, as provided in that agreement—was fixed.[58]

The future advances at issue here were made after that February 1969 date. (They consisted of Kimbell's continuing to extend credit to O.K. on open account, after O.K. had used the proceeds of the Bank's February 1969 loan to pay off its 1968 note to Kim-

[58] The participation of the SBA appeared from the face of the note (App. 70-71), though not from the security agreement and financing statement filed with the Secretary of State. Since Kimbell was fully aware of the SBA's participation in the loan (see *supra*, pp. 3-4; App. 61-64), it cannot claim that the lack of reference to the SBA in the security agreement and financing statement precluded the SBA's interest from attaching, at least in relation to Kimbell's lien, when the security agreement was filed.

bell (see p. 5, *supra*.)) The present case is therefore controlled by *United States* v. *R. F. Ball Construction Co., Inc.*, 355 U.S. 587 (*per curiam*). The Court there "rejected as inchoate an assignee's or mortgagee's lien to secure future indebtedness of the taxpayer-debtor." *United States* v. *Pioneer American Insurance Co.*, 374 U.S. 84, 91. In *R. F. Ball*, sums due the contractor-taxpayer under a construction contract were assigned to a surety as security for any future indebtedness of the contractor to the surety arising under that contract or any other (374 U.S. at 91). After the filing of the federal tax lien against the contractor, the surety made advances to complete another contract of the taxpayer, as it was obligated to do under its bond issued on that contract, and the contractor thereby became indebted to the surety. This Court held that the surety's interest securing these later payments was "inchoate and unperfected" at the time the federal tax lien was filed and was therefore junior to the tax lien (*ibid.*); see *United States* v. *R. F. Ball Construction Co., Inc.*, *supra*, 355 U.S. at 588-589 (Whittaker, J., dissenting).[59]

So, here, the future advances were made only after the federal lien attached. They were "uncertain in amount, and yet to be incurred and paid," in Febru-

[59] See also Rev. Rul. 56-41, 1956-1 Cum. Bull. 562, relating to advances of money by a mortgagee under an open-end mortgage, cited with approval in *United States* v. *Pioneer American Insurance Co.*, *supra*, 374 U.S. at 91-92, n.10. The Internal Revenue Service there ruled that a lien to secure advances by the mortgagee did not have priority over an intervening Federal tax lien.

ary 1969—Kimbell might or might not make them, having no obligation to do so—and Kimbell therefore held "merely a *caveat* of a more perfect lien to come, *New York* v. *Maclay*, 288 U.S. 290, 294." *United States* v. *Pioneer American Insurance Co.*, *supra*, 374 U.S. at 91.

B. But even if the SBA's lien did not attach until the note was assigned to the SBA by the Bank and this assignment was recorded, on January 21, 1971 (see pp. 5-6, *supra*), the SBA's lien is still senior to Kimbell's lien for the future advances.

When the Bank's assignment to the SBA was filed, on January 21, 1971, Kimbell had filed suit in state court on its claimed advances to O.K. (see p. 5, *supra*). But Kimbell's claim was not enforceable by summary proceedings, and the amount of its valid claim was open to dispute by O.K. until Kimbell reduced the claim to judgment on February 4, 1972 (see Pet. App. 23a-24a, n. 14; p. 6, *supra*; Pet. App. 33a n. 2). The amount of Kimbell's lien therefore was not certain, and the lien therefore was not choate, on January 21, 1971. *United States* v. *City of New Britain*, 347 U.S. 81; *United States* v. *White Bear Brewing Co.*, 350 U.S. 1010 (*per curiam*), 1010-1011 (Douglas, J., dissenting) (mechanic's lien held inchoate by the Court even though contract was completed, mechanic's lien was recorded in specific amount on specific property, and mechanic had instituted suit before federal lien attached). See

also *United States* v. *Vorreiter*, 355 U.S. 15; *United States* v. *Colotta*, 350 U.S. 808.[60]

In these circumstances, the SBA's lien is entitled to priority as the lien "first in time."[61]

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[60] These cases refute the suggestion of the court below (Pet. App. 23a-24a, n.14) that Kimbell's lien may have been choate before January 15, 1971, because Kimbell had "terminated extensions of credit" to O.K. before that date. In *White Bear Brewing Co.*, *supra*, the contract was completed and the mechanic had instituted suit to enforce his lien, but the mechanic's lien was nonetheless held to be inchoate, presumably because the amount actually due remained open to dispute, as in this case. The court below relied on *Crest Finance Co.*, *supra*, 368 U.S. 347, but that case is distinguishable because there the amount due was established by the face amount of the lienor's note.

With respect to respondent's claim for attorneys' fees (see pp. 5-6 and n. 7, *supra*), since its lien for the future advances that it recovered in the state court proceeding is not prior to the SBA's claim, its asserted lien for the attorneys' fees allowed in that proceeding cannot be. See *United States* v. *Liverpool & London Insurance Co.*, 348 U.S. 215, 217. The amount of fees was not fixed until the court's judgment setting the fees was entered, which did not occur until February 4, 1972 (App. 29). (Tex. Civ. Stat. Art. 2226 (1971) provides for "a reasonable amount as attorney's fees" in suits on a contract. The security agreement provided, in the event of default, "a reasonable attorney's fee not exceeding 10 percent of the unpaid principal and interest" (App. 17).) See *United States* v. *Pioneer American Insurance Co.*, *supra*, 374 U.S. at 87; cf. *United States* v. *Equitable Life Assurance Society of the United States*, 384 U.S. 323, 329. The lien for attorneys' fees therefore was not choate when the SBA's lien attached.

[61] If the court below had adopted the rules of the Federal Tax Lien Act of 1966 (see p. 49, n. 55, *supra*), it probably would have found that the SBA's lien had priority. The Act gives priority to future advances made pursuant to a written financing agreement only if they are made within 45 days

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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of the filing of the tax lien and before receipt of actual notice of that filing. 26 U.S.C. 6323(c)(2)(A). If the date of the Bank's filing of the security agreement and financing statement, February 18, 1969, is taken as the date when the SBA's lien attached, as the court below correctly held (Pet. App. 26a; see p. 52, *supra*), Kimbell would lose under the test of the 1966 Act for two reasons: it had actual notice of the SBA's interest in the loan at the time of the Bank's filing (see note 58, *supra;* App. 61-64), and it made at least some of its advances more than 45 days after that date (App. 47, 48-49, 61-64).

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In the

Supreme Court of the United States

OCTOBER TERM, 1978

No. 77-1359

UNITED STATES OF AMERICA,
Petitioner,

v.

KIMBELL FOODS, INC., *et al*,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR KIMBELL FOODS, INC.

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QUESTION PRESENTED

Whether a private contractual lien, created and perfected under state law, may be defeated by a junior private contractual lien, created and perfected under the same state law, by virtue of its subsequent assignment to an agency of the federal government?

STATEMENT

This case involves the relative priorities of two competing contractual security interests duly created and perfected under the UCC of Texas. The first party, Kimbell Foods,

Inc., ("Kimbell"), had duly acquired and perfected its security interest in accordance with state law in the collateral before the second party, Republic National Bank of Dallas, ("Republic"), had even acquired, much less perfected, a security interest in the same collateral. Over four years after Kimbell had first duly perfected its security interest, the SBA became a creditor of O. K. Super Markets, (the Debtor), and was at that point correspondingly assigned a portion of Republic's security interest. Under the Texas Uniform Commercial Code, the security interest granted Kimbell is clearly superior to the security interest granted Republic which was subsequently assigned to the SBA.

Kimbell, a grocery wholesaler, supplied inventory to O. K. on a weekly basis. In addition, in 1966 and 1968 Kimbell extended credit to O. K. evidenced by two promissory notes. In connection with the foregoing, O. K. and Kimbell entered into three separate security agreements. The first security agreement was executed in August, 1966, while the other two were executed in, respectively, April and November, 1968. In each of these security agreements O. K. granted Kimbell a security interest in certain grocery store equipment and fixtures and in "[a]ll goods, wares and merchandise and any and all additions or accessions thereto" which were located at specified locations. This collateral secured O.K.'s obligations to Kimbell under both notes as well as "all other indebtedness at any time hereafter owing by Debtor to Secured Party" including O. K.'s obligations to Kimbell for future inventory advances.

In September, 1966, and in April and November, 1968, Kimbell duly filed financing statements and the underlying security agreements with the office of the Texas Secretary of State. Under the Uniform Commercial Code as adopted

in Texas, this gave Kimbell a fully perfected security interest in the collateral which was senior to the interests of all other secured parties and lien creditors. In addition, it made the exact terms of the security agreements, including the future advance and after acquired property clauses, a matter of public record.

Subsequentiy, in February, 1969, O. K. obtained a $300,000.00 loan from Republic. This loan was secured by all of O. K.'s "machinery, fixtures, equipment and inventory, now existing or hereafter acquired" located at certain specific addresses, including those already covered by the Kimbell security agreements. Republic filed a financing statement with the Texas Secretary of State on February 18, 1969.

When Republic made its loan to O. K., Republic was aware that Kimbell held a senior security interest on certain of O. K.'s assets. Republic insisted that O. K. pay off all senior secured debts, but O. K. paid Kimbell only the remaining balance under the notes, leaving an outstanding balance of $18,390.93 for inventory purchases. No request was made that Kimbell file any termination statements or releases of its financing statements.

At the time O. K. sought the loan from Republic, both Republic and O. K. applied to the SBA for a guaranty of Republic's prospective loan to O. K. In connection therewith, Republic was required to submit to the SBA all relevant credit information on O. K. and on the collateral for the loan, including the nature of Kimbell's security interest in certain of O. K.'s assets. In addition, the SBA conducted its own appraisal of O. K.'s assets.

In January, 1969, the SBA agreed to guaranty 90% of Republic's loan to O. K. Neither at the time the SBA issued its guaranty to Republic, nor at the time Republic made its

loan to O. K., did the SBA advance any funds to O. K. or Republic. In 1969 the SBA therefore was not a secured party with an interest in the collateral, but was a guarantor with a contingent claim against O. K. No reference to the SBA guaranty appeared in Republic's security agreement or financing agreement or financing statement (App. 67-69).

For approximately two years thereafter, Kimbell continued to supply inventory to O. K. in reliance upon Kimbell's senior security interest, as determined by the respective filings of Kimbell and Republic with the office of the Texas Secretary of State. After January 15, 1971, however, Kimbell ceased supplying O. K. with inventory and received no further payments from O. K. At this time, just as at all times in preceding years, Kimbell's security interest was certain in all respects: Kimbell's identity as a secured party was a matter of public record, the identity of the collateral was fixed, and the amount of Kimbell's claim was liquidated.

Three weeks later, on February 3, 1971, O. K. and Republic agreed to a sale of all the assets of O. K. located at three of O. K.'s stores, with the proceeds of such sale to be held in escrow by Republic pending resolution of competing claims to such fund. This agreement was approved by the SBA and Kimbell. Subsequently, the contents of the three stores were sold for an aggregate purchase price of $95,000.00.

Also on February 3, 1971, the SBA honored its guaranty and paid $252,331.93 to Republic, which amount represented 90% of O. K.'s then outstanding indebtedness to Republic. This was the first time that SBA funds were advanced in connection with Republic's loan to O. K. As such, the SBA, up to this time a contingent unsecured creditor, acquired an interest in the loan through the purchase of the note held by Republic.

On February 4, 1972, Kimbell obtained a judgment in state court against O. K. in the amount of $24,445.37. This represented the exact amount of the O.K.'s principal indebtedness to Kimbell ($18,258.57), plus interest ($1,186.80) and attorneys' fees ($5,000.00). Kimbell then filed the present suit in the United States District Court for the Northern District of Texas seeking a declaration that its security interest in certain of O. K.'s property created a claim to the escrow fund which was senior to the claims of Republic and the SBA, and asking for judgment against Republic as escrowee.

The United States District Court found Kimbell's security interest inferior to that of the SBA, and Kimbell appealed the District Court ruling to the Circuit Court of Appeals for the Fifth Circuit which court reversed the District Court. Subsequently the United States petitioned this court for a writ of certiorari, which writ was granted.

ARGUMENT

I. THE APPELLATE COURT WAS CORRECT IN HOLDING THE CHOATE LIEN DOCTRINE INAPPLICABLE IN DETERMINING THE PRIORITY OF KIMBELL FOODS' SECURITY INTEREST

A. The Policies and Circumstances Which the Choate Lien Doctrine is Applicable to Are Not Present in This Instance

The choate lien doctrine had its genesis in decisions involving the application of the federal insolvency priority statute, (R.S. 3466, now 31 U.S.C. 191) to federal tax liens. *New York v. MaClay*, 288 U.S. 290, *United States v. Texas*, 314 U.S. 480, *United States v. Waddill, Holland & Flinn, Inc.*, 323 U.S. 353, *United States v. Gilbert Associates, Inc.*, 345 U.S. 361.

The doctrine was extended in *United States v. Security Trust & Savings Bank*, 340 U.S. 47 to determine the priority of a federal tax lien arising outside the context of the federal insolvency priority statute, and was subsequently applied in similar circumstances to a miscellany of statutory liens. *United States v. City of New Britain*, 347 U.S. 81, *United States v. Acri*, 348 U.S. 211, *United States v. White Bear Brewing Company*, 350 U.S. 1010, *United States v. Liverpool & London Insurance Co.*, 348 U.S. 215, *United States v. Colotta*, 350 U.S. 808, *United States v. Vorreiter*, 355 U.S. 15, *United States v. Vermont*, 377 U.S. 351, *U. S. v. Equitable Life Assurance Society of the United States*, 384 U.S. 323.

The government in its brief identifies the underlying policy of the federal insolvency priority statute to be ". . . securing an adequate revenue to sustain the public burthens and discharge the public debts", and recognizes that the development of the choate lien doctrine within the context of the federal insolvency priority statute was to secure those broad revenues (Petitioner's brief page 17).

In *United States v. Security Trust & Savings Bank*, 340 U.S. 47, this court analogizes the purpose of the federal insolvency priority statute to the purpose of federal tax liens and concludes that a rule similar to the rule for determining priorities in the context of the federal insolvency priority statute must also prevail in the area of federal tax liens (340 U.S. at 51).

Tax revenues contribute overwhelmingly to the general treasury fund which funds the expenses incurred by government in exercising both its constitutional and non-constitutional functions. The continued existence of the sovereign is dependent upon its ability to lay and collect taxes.

The choate lien doctrine was extended to the area of federal tax liens in recognition of these paramount policies,

to insure that the power of the sovereign to lay and collect taxes is unimpeded. No such policy considerations are here present.

The government attempts to equate Small Business Administration revenues with tax revenues (Petitioner's brief page 22), and analogize Small Business Administration lending activities to a constitutional function of government (Petitioner's brief pages 24, 25). The equation, however, is unbalanced and the analogy incorrect.

Unlike tax revenues which fund both the constitutional and non-constitutional functions of government, Small Business Administration revenues are earmarked for funding additional loans by the Small Business Administration. 15 U.S.C. 633(c).

Clearly tax revenues are of far greater significance and importance to the sovereign than Small Business Administration revenues.

It is an axiom of American jurisprudence that certain property rights are of greater importance than others and deserving of greater safeguards. As a voluntary lender with a pre-existing opportunity to evaluate credit risks, the government is not entitled to the greater safeguards afforded it as an involuntary creditor of a tax delinquent.

No decision of this court has extended the choate lien doctrine outside the area of federal tax liens. No court of appeals has yet found it necessary to employ the choate lien doctrine in determining the priority of a federal consensual security interest competing with a prior perfected security interest. *Chicago Title Insurance Co. v. Sherred Village Associates*, 568 F. 2d 217, petition for certiorari pending sub nom., *Herco-Form Incorporated v. Chicago Title Insurance Co.* (No. 77-1611), *United States v. General Doug-*

las MacArthur, Sr. Village, Inc., 470 F. 2d 675, cert. den. sub nom, *County of Nassau v. United States*, 412 U.S. 922, *United States v. Ringwood Iron Mines*, 251 F. 2d 145, *H. B. Agsten & Sons, Inc. v. Huntington Trust & Savings Bank*, 388 F. 2d 156, cert. den. 390 U.S. 1025, *United States v. County of Iowa*, 295 F. 2d 257, *Willow Creek Lumber Company, Inc. v. Porter County Plumbing & Heating, Inc.*, 572 F. 2d 588, *United States v. Latrobe Construction Co.*, 246 F. 2d 357, cert. den. 355 U.S. 890, *Southwest Engine Co. v. United States*, 275 F. 2d 106, *Director of Revenue, State of Colorado v. United States*, 392 F. 2d 307, *T. H. Rogers Lumber Co. v. Apel*, 468 F. 2d 14. In each of the foregoing cases the federal lien had arisen prior to the lien or liens with which it was competing, and in each instance the federal lien was competing with a non-consensual lien acquiring an artificial priority not determined by a notice filing system.

Other courts have recognized the impropriety of extending the choate lien doctrine outside the area of federal tax liens. *Hammer v. Chapin*, 256 F. Supp. 818, *Ault v. Harris*, 317 F. Supp. 373, affirmed 432 F. 2d 441 and *United States v. California-Oregon Plywood, Inc.*, 527 F. 2d 687.

The choate lien doctrine is a doctrine of limited applicability which was designed to protect property interests of particular significance to the sovereign. No valid policy considerations exist for extending the choate lien doctrine beyond the limited circumstances and policies which have necessitated its application.

In 1966 Congress limited and severely restricted the application of the choate lien doctrine in the area of federal tax liens, Federal Tax Lien Act of 1966, the only area that this court has held the doctrine applicable to outside the context of the federal insolvency priority statute.

The extension of the choate lien doctrine beyond the area of federal tax liens has been the subject of significant criticism by legal commentators. Plumb, *Federal Liens and Priorities — Agenda for the Next Decade*, 77 Yale Law Journal 228, (1967); 2 G. Gilmore, *Security Interests in Personal Property* Sections 40.3 to 40.6 (1965); Kennedy, *The Pernicious Career of the Inchoate and General Lien*, 63 Yale Law Journal 906 (1954); Kennedy, *From Spokane County to Vermont: The Campaign of the Federal Government Against The Inchoate Lien*, 50 Iowa Law Review 755 (1965).

In the absence of a statute or decision by this court to the contrary, the court of appeals correctly determined that Kimbell was "first in time" by looking to the priority of perfection under the Uniform Commercial Code and in refusing to create a rule of law based upon the misapplication of the choate lien doctrine.

B. *"A Uniform and Certain Means Exists to Determine Lien Priorities in the Area of Government Liens Arising From Consensual Lending Activities*

The Uniform Commercial Code was created as a series of model laws establishing rights and obligations between parties involved in commercial transactions. It has been recognized as being "... on its way to becoming a truly national law of commerce, . . . more complete and more certain than any other which can conceivably be drawn from the sources of 'general law' . . . and . . . when the states have gone so far in achieving the desirable goal of a uniform law governing commercial transactions it would be a distinct disservice to insist on a different one for the segment of commerce important but still small in relation to the total, consisting

of transactions with the United States," *United States v. Wegematic Corp.*, 360 F. 2d 676.

Article 9 of the Uniform Commercial Code which governs rights and obligations between a debtor and competing creditors has been enacted with minor variations in 49 states as well as the District of Columbia. In order to provide competing creditors of a debtor with sufficient information to determine the priority of their security interests and evaluate their security risks, each state maintains a notice filing system as a part of their public records. These notice filing systems serve the principle that as between voluntary creditors the "first in time" should prevail, the same principle which has been a companion doctrine to the choate lien doctrine.

The choate lien doctrine was created at a time when there was no uniform national notice filing system for determining relative priorities among consensual competing creditors, and was applied to liens of a peculiarly local nature, whose priority was not governed by a uniform notice filing system.

The court of appeals has recognized the reliance of the commercial world on Article 9 of the Uniform Commercial Code and its provisions governing notice filing systems and has correctly applied it as the appropriate means for determining priorities between competing consensual creditors.

Since its inception, the provisions of Article 9 have become increasingly uniform as time and judicial interpretation have led to established expectations among parties whose affairs are governed by its provisions and whose contractual expectations are drafted in accordance with its rules.

The choate lien doctrine, on the contrary, has evolved from the reversal of decisions of lower courts in which it was misapplied. *United States v. Pioneer American Insurance Co.*, 374 U.S. 84, *United States v. R. F. Ball Construction Co., Inc.*, 355 U.S. 587 (per curiam), *United States v. Vorreites*, 355 U.S. 15 (per curiam), *United States v. Colotta*, 350 U.S. 808. It is supported by a relatively small and incomplete body of precedent and its application outside the context of the federal insolvency priority statute has resulted in differing standards. *United States v. City of New Britain*, 347 U.S. 81, *United States v. Vermont*, 377 U.S. 351.

To reject the established provisions of the Uniform Commercial Code directly applicable to the affairs of lenders and borrowers, in favor of an inapplicable and uncertain doctrine would be illogical in itself. However, other compelling considerations dictate against the adoption of the choate lien doctrine in this instance.

Were the choate lien doctrine held to be applicable in instances such as this, then non-government, secured and perfected lenders would face the prospect that their security could be defeated by the later acquisition of a junior security interest by the federal government either directly or by assignment. The ramifications of that prospect would extend throughout commerce, upsetting the stability and uniformity in lending transactions established by Article 9 of the Uniform Commercial Code, and altering the contractual expectations of debtor and lender alike. One foreseeable result would be a severe curtailment of credit by the non-government lending sector and attendant severe economic dislocation.

This court in *Aquilino v. United States*, 363 U.S. 509 endorsed the principle that if a state does not recognize a property interest in a debtor sufficient to sustain a lien, that no lien can attach, in effect recognizing that the choate lien doctrine should be governed by the right of the states to

define the existence of property interests. Were the choate lien doctrine held to be applicable in determining priorities between competing consensual lenders, then creditors with a prior perfected security interest could be divested of those property interests by a federal doctrine which purports not to interfere with state-created property interests. Such a holding would be in conflict with this court's construction of the perimeters of the choate lien doctrine recognized in *Aquilino v. United States, supra.*

Any questions of priority left unresolved by the application of the Uniform Commercial Code in this instance by the court of appeals would be insignificant in comparison to the unresolved questions of priority which would come into existence were the choate lien doctrine to be extended to instances such as this.

The Small Business Administration in receiving its revenues from a broad base of consensual debtors is in a better position to self-insure its rights than are private parties for some of whom the failure of even a single major debtor may be ruinous. "It is hardly sound government policy to attempt to bolster the economy by federal loans and guarantees and at the same time to discourage uninsured credit by making it more hazardous." MacLachlan, *Improving the Law of Federal Liens and Priorities*, 1 B.C. Ind. and Com. L. Rev. 73, 74-76 (1959).

The Small Business Administration suffers no prejudice or burden by being required to examine the notice filing systems in effect throughout the United States. Indeed such examination is indispensable to a determination of whether a Small Business Administration loan is "of such sound value or so secured as reasonably to assure repayment", 15 U.S.C. 636(a) (7), and such requirement may be viewed as indicative of an intent that the Small Business

Administration function no differently than other commercial lenders. Should the Small Business Administration then find a creditor senior to itself, it can request subordination and if subordination is not forthcoming, then determine whether the loan is appropriate within the meaning of 15 U.S.C. 636(a) (7).

II. KIMBELL'S SECURITY INTEREST IS SUFFICIENTLY CHOATE TO PREVAIL OVER THE SMALL BUSINESS ADMINISTRATION'S SECURITY INTEREST

The security interests of Kimbell Foods, Inc. were duly perfected in accordance with state laws patterned after Article 9 of the Uniform Commercial Code. Notice of those security interests had been duly filed by 1968, prior to the loan by Republic National Bank of Dallas to O.K. Super Markets in 1969.

At any given instant that security interest was fully choate within the perimeters of the choate lien doctrine as established by *United States v. City of New Britain*, 347 U.S. 81.

It is undisputed that Kimbell Foods, Inc. was reflected of record as claiming a security interest in the assets which are the subject matter of this controversy prior to any Small Business Administration involvement with O. K. Super Markets.

The certainty of a debt varies with the nature of the debt. Accordingly the certainty of different debts is established in different manners. Unlike varying statutory liens which may or may not be established prior to judgment depending upon when various elements of such debts are established, at any given instant the debt of O. K. Super

Markets to Kimbell Foods, Inc. was a fixed liquidated sum established by the difference between the aggregate of the sums advanced by Kimbell Foods, Inc. to O. K. Super Markets and the aggregate repayments by O. K. Super Markets to Kimbell Foods, Inc.

CONCLUSION

In light of the policy considerations which have limited the applicability of the choate lien doctrine and in recognition of both the judicial and legislative policies which have led to its curtailment outside the context of federal tax liens, the court of appeals correctly employed the Uniform Commercial Code in this instance to determine the relative priority of competing consensual security interests, one held by the federal government by virtue of an assignment from a non-government commercial lender, and the other by a non-government commercial lender. The judgment of the court of appeals should be upheld.

Respectfully submitted,

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October, 1978

No. 77-1359

In the Supreme Court of the United States

OCTOBER TERM, 1978

UNITED STATES OF AMERICA, PETITIONER

v.

KIMBELL FOODS, INC., ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

REPLY BRIEF FOR THE UNITED STATES

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I

Respondent and amicus curiae National Commercial Finance Conference, Inc., urge this Court to affirm the decision of the court of appeals by applying the Uniform Commercial Code (U.C.C.) provisions on lien priority to contests between federal contractual liens and private consensual liens. Respondent states that the court of appeals "has correctly applied [the U.C.C.] as the appropriate means

for determining priorities between competing consensual creditors" (Resp. Br. 10; see also *id.* at 9). Amicus, stating that the court of appeals "adopt[ed] one aspect of the Code to resolve the question in this case," urges this Court to embrace "complete reliance upon the perfection and priority rules of Article 9 * * *" as the rule of law governing cases such as this (Amicus Br. 24; see generally *id.* at 22–30).[1]

But the court of appeals, in according priority to respondent's lien, did not adopt the priority rule of the U.C.C. It expressly held back from doing so. On the ultimate question of "the substantive content of the 'first in time, first in right' rule with regard to future advances" (Pet. App. 26A), the court considered three rules followed by various states prior to enactment of the U.C.C., one of which—the rule freely allowing relation-back of optional future advances—was the rule adopted by the U.C.C. (Pet. App. 27A–28A & n.17). "[I]n crafting federal common law for this case," the court found no need to do more than determine that

[1] Amicus cites (Br. 23) cases in which, it claims, the courts have applied the U.C.C. as the "federal law merchant." Other than *United States* v. *Wegematic Corp.*, 360 F.2d 674 (2d Cir. 1966), the cited cases either arose in the Fifth or Ninth Circuits, which have rejected the choate lien doctrine in any event, or did not involve the United States as a party or did not apply the U.C.C.

Wegematic involved the choice of a federal rule when a federal contractor claims excuse for failure to perform a contract. The court of appeals that decided *Wegematic* has since expressly refused to abandon the choateness requirement for federal contractual liens. *United States* v. *General Douglas MacArthur Senior Village, Inc.*, 470 F.2d 675 (2d Cir. 1972), cert. denied, 412 U.S. 922 (1973).

respondent's lien would relate back "under either the actual notice rule or the U.C.C. rule" (Pet. App. 28A). The court observed that "[s]trong policy arguments favoring greater protection for the SBA counsel adoption of the actual notice rule while equally strong considerations * * * urge adoption of the U.C.C. rule," and it reserved "the final resolution of this difficult decision for another day" (Pet. App. 28A n.18).

Thus, respondent and amicus are urging this Court to adopt a rule that the court below considered but deliberately avoided adopting in this case.

There are important reasons why this Court should not adopt, as a rule of federal common law affecting contractual liens of the United States, the U.C.C. rule on relation-back of optional future advances.[2] As the court of appeals recognized, "strong policy arguments" support protection for federal liens; if those arguments are to be rejected, and the property interests of the United States subordinated to competing interests, Congress should make that decision. Like the federal tax liens protected by this Court through the choateness doctrine in cases such as *Security Trust* and *City of New Britain*,[3] a federal contractual lien is a vested federal property interest that should not be reduced or

[2] The Court also should not adopt the picking-and-choosing approach of the court of appeals, which abandons the well-established choateness rule in favor of ad hoc uncertainty and gives inadequate protection to federal property interests. See our main brief at 37–51.

[3] *United States* v. *Security Trust & Savings Bank*, 340 U.S. 47, 51 (1950); *United States* v. *City of New Britain*, 347 U.S. 81, 85–86 (1954); see our main brief at 16–25.

superseded by state law rules of priority unless Congress so provides.[4]

When Congress in the 1966 Federal Tax Lien Act (26 U.S.C. 6323) did consider and alter the priorities of federal tax liens, it rejected the approach of adopting the U.C.C. or other state law and instead fashioned its own rules (see our main brief at 47–49). Of particular pertinence here, Congress dealt specifically with the subject of liens for future advances. It gave such liens priority over federal tax liens only to the extent that the future advances are made within 45

[4] This is particularly clear where, as here, the state law would create priority for the non-federal lien by providing that optional advances made subsequent to attachment of the federal lien "relate back" to obtain a security interest dating from before the federal lien. With respect to private consensual liens competing with federal tax liens, this Court has refused to apply "the long since rejected relation-back doctrine." *United States* v. *Pioneer American Insurance Co.*, 374 U.S. 84, 92 n.11 (1963). Absent congressional intervention, the doctrine equally deserves rejection when applied to undercut federal contractual liens. There is, indeed, an Alice in Wonderland quality about some of the relation-back claims of respondent and amicus. For instance, amicus argues (Br. 36) that a future-advancing party such as respondent should not have "to speculate whether a junior security interest may someday be created and sold to the government and be catapulted to senior status through the retroactive application of the choateness doctrine." It is not easy to relate this statement to the facts that the $300,000 loan to O.K. Super Markets by the Bank—which enabled O.K. to pay off its existing indebtedness to respondent—was made and secured, and the SBA's guarantee of that loan was known to respondent, not "someday" but *before* respondent made the optional future advances of inventory for which respondent now claims a lien prior to that of the bank loan. See also, *e.g.*, Amicus Br. 28, 42–43.

days of the filing of the tax lien and before receipt of actual notice of that filing. 26 U.S.C. 6323(c)(2)(A); see W. T. Plumb, *Federal Tax Liens* 92 (1972).[5] Thus, Congress adopted the "actual notice" rule, and it further placed a strict time limit on the future advances that would be protected against the prior federal tax lien. In contrast, under the U.C.C. rule that respondent and amicus urge this Court to adopt, any future advances made to the debtor by respondent would take priority over the federal contractual lien securing a loan made before the advances. See Texas Bus. & Com. Code 9.312(e)(1) and Comment, Example 4: *id.*, 9.204(e) (1968); *id.*, 9.312(g) (1978 Supp.) (Texas U.C.C.). The U.C.C. rule would subordinate federal contractual liens to a much greater extent than Congress was willing to subordinate federal tax liens. If such a waiver of federal property interests is to take place, Congress, not this Court, should make the decision.[6]

[5] In addition, the competing lien loses its priority with respect to new collateral acquired by the borrower more than 45 days after the filing of the tax lien. 26 U.S.C. 6323(c)(2)(B); W. T. Plumb, *supra*, at 92 (1972).

[6] This conclusion draws further support from the provision of the Small Business Act, 15 U.S.C. 646, in which Congress in 1958 considered the priority of SBA liens and withdrew that priority only as against state and local liens for property taxes (see our main brief at 33–37). Amicus quotes from the SBA's 1958 letter to Congress (Amicus Br. 11) the inadvertently incorrect statement that the priority of the United States under the insolvency statute, 31 U.S.C. 191, "is not applicable to property which is subject to a lien of any kind." Compare the decisions of this Court cited in our main brief at 18–19 nn.

II

Respondent and amicus see dire consequences from application of the choate lien doctrine to cases such as this (Resp. Br. 11; Amicus Br. 7, 28). They foretell

(Continued)

15–19; see also, *e.g.*, *City of Sherman* v. *United States*, 400 F.2d 373, 377 (5th Cir. 1968). The statement is in any event irrelevant here. The SBA letter went on to propose the bill which was enacted as 15 U.S.C. 646 and which provided, without reference to the insolvency statute, that any security interest of the SBA shall be subordinate to any state or local lien for property taxes that would take priority under local law if the SBA lien were held by a private party. In so proposing, the SBA Administrator noted the recent decision of the Third Circuit in *United States* v. *Ringwood Iron Mines, Inc.*, 251 F.2d 145 (1958), holding "that a mortgage lien held by the United States stands in the same position as a tax lien held by the United States * * *." *Hearings on Credit Needs of Small Business Before a Subcomm. of the Senate Comm. on Banking and Currency. 85th Cong., 2d Sess.* 554 (1958). The decision in *Ringwood Iron Mines* was expressly based on this Court's decision in *United States* v. *City of New Britain*, 347 U.S. 81 (1954), which definitively reaffirmed the choateness doctrine (*id.* at 84, 86–87).

Thus the 1958 statute waived in favor of state and local property tax liens the priority to which SBA liens were entitled under the first-in-time and choateness rules. As the court of appeals acknowledged (Pet. App. 21A n.13)—though the court chose a different view (*ibid.*)—"[t]his statute could be read as ameliorating the impact of the choateness doctrine by waiving the immunity it would grant, thus implicitly recognizing the applicability of the choateness doctrine to SBA liens." Moreover, the action of Congress in 1958 in specifically addressing the question of SBA lien priority and removing that priority in only a narrow and precisely tailored fashion, like its action in the Federal Tax Lien Act of 1966, underlines the inappropriateness of this Court's revamping on a wholesale basis the priorities of SBA liens and of federal contractual liens generally.

"a severe curtailment of credit by the non-government lending sector and attendant severe economic dislocation" (Resp. Br. 11). More particularly, they contend that "a lender providing revolving credit secured by accounts receivable or inventory" will be required, on learning of the government's involvement in a loan to the debtor, "to terminate financing and liquidate its collateral to preserve its priority position," with the usual result of "destroying the borrower's business" and causing irreparable injury to the lender as well (Amicus Br. 7).

These fears are extravagantly overdrawn. The choate lien doctrine has been the law for many years, both with respect to federal tax liens under this Court's decisions and with respect to federal contractual liens under the decisions of most of the circuits (see our main brief at 26–27 and 39 n.43), without evidence of any adverse consequence to lenders or borrowers. In 1950 this Court first applied the choateness rule to determine the priority of federal tax liens (*United States* v. *Security Trust & Savings Bank*, 340 U.S. 47, 51); and amicus states (Br. 6) that "[t]he annual volume of financing by the commercial finance and factoring industry has increased from approximately $5,000,000,000 in 1950 to over $70,000,000,000 in 1970." This is not the record of an industry crimped and oppressed by a hostile rule of law. Neither amicus nor respondent has offered any evidence—and the SBA is aware of none (see our main brief at 43 n.49)—suggesting that commercial lending in jurisdictions applying the choateness rule has been inhibited

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or reduced in comparison with jurisdictions not applying that rule, or reporting any ill effects during the decade when the rule prevailed in the Fifth Circuit itself.[7]

As for the lender who is providing revolving credit secured by accounts receivable or inventory and discovers that the government is lending money to the same debtor, there is no cause, so long as he contemporaneously receives notes or comparable instruments evidencing specific amounts of definite indebtedness, for him to fear for the priority of advances he made before the government entered the picture. See *Crest Finance Co.* v. *United States,* 368 U.S. 347, (1961); cf. W. H. Plumb, *Federal Tax Liens* 64 (1961), citing Rev. Rul. 56–41, 1956–1 Cum. Bull. 562. With respect to optional future advances, the lender can evaluate the borrower's financial position in light of both the infusion of funds from the government and the security interest taken by the government, and on that basis can determine whether to continue making advances.

In this case, for example, the $300,000 bank loan to O.K. Super Markets in February 1969 that was guaranteed by the SBA—as Kimbell knew it was guaranteed—enabled O.K. to pay off the approximately $25,000 it then owed Kimbell and subsequently to pay Kimbell more than $18,000 for new inventory over the next two years, while incurring a new balance of some $18,000 on open account (see our main

[7] Compare *United States* v. *Roessling*, 280 F.2d 933 (5th Cir. 1960), with *Connecticut Mutual Life Insurance Co.* v. *Carter*, 446 F.2d 136 (5th Cir.), cert. denied, 404 U.S. 857 (1971).

brief at 5). These events took place prior to June 1971, when the Fifth Circuit in the *Connecticut Mutual* case (446 F.2d 136) rejected the choateness doctrine which it had espoused in the 1960 *Roessling* case (280 F.2d 933). That doctrine thus apparently did not deter Kimbell from making future advances with knowledge of the government's involvement. Nor do these facts seem atypical. To the extent that the government's financial assistance serves its intended purpose of improving the financial standing of the borrower, the private lender should find it no less attractive to do business with the borrower after the government makes its secured loan than before.[8]

Amicus states (Br. 6) that secured lenders "know that their security interests will be inferior to earlier perfected liens and security interests" and "therefore review the appropriate public records to determine the relative priority of their security interests in the collateral."[9] If this is so, it is hard to see why a lender/supplier such as Kimbell in this case should be preju-

[8] If the private lender is really unwilling to advance funds to a borrower who might subsequently obtain federal financial assistance involving a federal security interest, the lender can condition its own loan on a requirement that the borrower obtain the private lender's consent before accepting federal financial assistance.

[9] But cf. Note, *Priority of Future Advances Lending Under the Uniform Commercial Code*, 35 U. Chi. L. Rev. 128, 143 (1967): "it has been repeatedly stated that in practice lenders seldom check public records for claims on the borrower's assets. Instead, they rely on credit-rating services to supply information about financial standing." (Footnote citing authorities omitted.)

diced or deterred by a rule of law giving priority to a secured bank loan that Kimbell knew the SBA had guaranteed, and that was perfected and recorded before Kimbell made the advances for which it here claims priority. Perhaps, however, amicus and respondent would say it is inconvenient for a creditor or supplier to search the public records regularly, in order to ascertain whether there is an intervening federal lien, before making advances. But any such inconvenience apparently already exists, since federal tax liens continue to take priority over most subsequent advances (see pages 4–5, *supra*), and regular searches must be made for such liens.[10] Moreover, the same necessity prevailed under this Court's earlier decisions applying the choateness doctrine in the context of federal tax liens, and lenders nevertheless succeeded in protecting themselves. See W. T. Plumb, *Federal Tax Liens* 64 (1961). A lender's reluctance to take steps—or have its credit agency take steps—to determine whether it is dealing with the federal government before it makes additional advances thus is not an adequate reason for abandoning the choate lien doctrine and the federal interests that it protects.[11]

[10] The inconvenience may be minimal, however, if lenders rely on credit agencies to do the searching. See note 9, *supra*.

[11] Lenders must also contend with other liens that may intervene after the initial financing agreement is perfected and take priority over future advances, such as state or local tax liens or mechanic's or repairman's liens accorded superpriority by local law. There is no evidence that these have appreciably deterred the growth of commercial financing or revolving credit.

III

Confronted with the unanimous authority in the courts of appeals prior to the Federal Tax Lien Act of 1966 applying the first-in-time and choateness rules in the context of federal contractual liens (see our main brief at 26), and the adherence to those rules by the great majority of the courts of appeals since the 1966 Act (see *id.* at 27 and 39 n. 43), respondent and amicus attempt to distinguish these cases. They claim, first, that the decisions do not reflect application of the choateness doctrine because the same result could have been reached by applying the first-in-time rule alone (Resp. Br. 7–8; Amicus Br. 10, 19).

But the first-in-time rule cannot be applied without corollary rules for determining the time when a lien is created, and the courts of appeals have expressly chosen the choateness rule for this purpose.[12] In a number of the cases, application of the state rule instead would have rendered the non-federal lien first in time.[13] It was therefore not surplusage when these

[12] *E.g.*, *Willow Creek Lumber Co.* v. *Porter County Plumbing & Heating, Inc.*, 572 F.2d 588, 591 (7th Cir. 1978); *Chicago Title Insurance Co.* v. *Sherred Village Associates*, 568 F.2d 217, 222 (1st Cir. 1978), petition for cert. pending *sub nom. Hercoform, Inc.* v. *Chicago Title Insurance Co.* (No. 77–1611); *T. H. Rogers Lumber Co.* v. *Apel*, 468 F.2d 14, 18–19 (10th Cir. 1972); *United States* v. *Oswald & Hess Co.*, 345 F.2d 886, 888 (3d Cir. 1965); *In re Lehigh Valley Mills, Inc.*, 341 F.2d 398, 401 (3d Cir. 1965).

[13] See, *e.g.*, *Chicago Title Insurance Co.* v. *Sherred Village Associates*, *supra*, 568 F.2d at 219 (contract executed before federal mortgage would have priority under state law); *T. H.*

courts stated that they were applying the choate lien test to determine which lien was first in time.

Respondent and amicus also claim to find it significant (Resp. Br. 8; Amicus Br. 19, 21) that none of the court of appeals cases applying the choate lien doctrine have involved a federal contractual lien and "a competing mortgage or perfected security interest created under Article 9 of the U.C.C." (Amicus Br. 19). But the reasoning of the decisions leaves little doubt that the courts of appeals applying the choate lien rule in the context of federal contractual liens would not distinguish between competing private liens created by particular statutes and competing private "consensual" liens created under the U.C.C. These courts have generally reasoned that the choate lien doctrine should be applied with respect to federal contractual liens by virtue of the authority and the reasoning of this Court's cases applying the doctrine with respect to federal tax liens.[14] And this Court in apply-

Rogers Lumber Co. v. *Apel*, *supra*, 468 F.2d at 16, 18 (lien for materials furnished before federal lien attached would have priority under state law); *In re Lehigh Valley Mills, Inc.*, 341 F.2d 398, 401 (3d Cir. 1965), reversing 225 F. Supp. 494, 496 (E.D. Pa.) (corporation taxes vested under state law before federal lien perfected).

[14] See, *e.g.*, *United States* v. *General Douglas MacArthur Senior Village, Inc.*, *supra*, 470 F.2d at 678–679; *T. H. Rogers Lumber Co.* v. *Apel*, *supra*, 468 F.2d at 20; *Director of Revenue, State of Colorado* v. *United States*, 392 F.2d 307, 312–313 (10th Cir. 1968); *United States* v. *Oswald & Hess Co.*, *supra*, 345 F.2d at 888; *United States* v. *County of Iowa*, 295 F.2d 257, 259 (7th Cir. 1961); *United States* v. *LATrobe Construction Co.*, 246 F.2d 357, 365 (8th Cir. 1957).

While dicta in *Chicago Title* suggest that the First Circuit might distinguish between privately-held secured interests and

ing the doctrine in that context has not distinguished between private statutory and private consensual liens. As amicus concedes (Br. 16–17), the Court has regularly applied the choate lien test to non-federal liens that arose by the consent of the parties. *United States* v. *Pioneer American Insurance Co.*, 374 U.S. 84 (1963); *Crest Finance Co.* v. *United States*, 368 U.S. 347 (1961); *United States* v. *Ball Construction Co.*, 355 U.S. 587 (1958).

The purpose of the choate lien doctrine is to prevent the government's vested property interests from being superseded by later-arising interests, and the source or nature of the non-federal interest is not determinative of whether it was certain and perfected at the time the federal lien attached.[15]

statutory liens because it views the U.C.C. as providing a usable, uniform rule (568 F.2d at 222), that court's basic rationale, that changes in "this arena of complex relationships" are best left to Congress (568 F.2d at 221), would appear to be at odds with such a distinction.

[15] Respondent asserts (Br. 11–12) that *Aquilino* v. *United States*, 363 U.S. 509 (1960), precludes application of the choate lien doctrine here. That case held that state law controlled the question "whether and to what extent the taxpayer had 'property' or 'rights to property' to which the tax lien could attach" (*id.* at 512). The Court went on to make it clear (*id.* at 513–514) that "once the tax lien has attached to the taxpayer's state-created interests, we enter the province of federal law, which we have consistently held determines the priority of competing liens asserted against the taxpayer's 'property' or 'rights to property'" (citing, *e.g.*, *United States* v. *Security Trust & Savings Bank*, *supra*, 340 U.S. 47, and *United States* v. *City of New Britain*, *supra*, 347 U.S. 81). In this case the question is the priority of competing liens attaching to admitted property rights, and as *Aquilino* recognized, that question is controlled by federal law.

IV

A. Respondent and amicus argue (Resp. Br. 13–14; Amicus Br. 37–41) that respondent's lien was choate at all relevant times and therefore has priority. They contend that the amount of the lien was certain because, like the amount of the debts evidenced by the notes in *Crest Finance Co.* v. *United States, supra,* 368 U.S. 347, it could be determined "from the books and records of the parties" (Amicus Br. 39; see Resp. Br. 13–14). They assert that "no judgment is required to make a fixed contractual debt of this kind certain in amount" (Amicus Br. 40).

Crest Finance, in which the government conceded that the competing lien was choate, and the Court agreed, is not the controlling precedent here. In *Crest,* nine loans were made, each evidenced by the taxpayer's note. Memorandum for the United States in *Crest Finance, supra,* at 3. While a substantial part of the aggregate principal amount of the notes had been repaid by the taxpayer (*ibid.*), this fact was evidently considered irrelevant, receiving no consideration in either the Memorandum for the United States or the opinion of the court of appeals (291 F.2d 1). The basis for the government's concession that the lien was choate was that "the notes" rendered the "amount

of the lien" specific and definite.[16] The assignments that constituted the collateral "were made to secure payment of notes in specific amounts for loans made contemporaneously with the assignments" (*id.* at 5). The lien "was for the liquidated amount of the notes evidencing the loans from petitioner to the taxpayer" (*id.* at 6). Thus, in *Crest,* the lienor had advanced money to the taxpayer, and the amount of the lien was specifically and definitely evidenced by the face value of notes signed by the taxpayer.

Here, notwithstanding the reference by amicus to "the notes in this case" (Br. 39), the future advances for which respondent claims a prior lien were not evidenced by any notes. Nor was their amount evidenced by any comparable documents signed by the debtor.[17] Further, the advances were not of money,

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[16] "Thus the lien fully met the requirements, enunciated by this Court, that it be specific and definite in three essential respects: (1) the identity of the lienholder (petitioner); (2) the amount of the lien (the notes); and (3) the property to which it attaches (the accounts receivable for the work already performed under the specific contract). *E.g., United States* v. *New Britain,* 347 U.S. 81." Memorandum for the United States, *supra,* at 5.

[17] Respondent says the amount owed was "at any given instant * * * a fixed liquidated sum established by the difference between the aggregate of the sums advanced by Kimbell Foods, Inc. to O.K. Super Markets and the aggregate repayments by O.K. Super Markets to Kimbell Foods, Inc." (Br. 13–14).

The Court of appeals said that Kimbell had terminated extensions of credit so that its accounts reflected the final amount of the claim secured by its security agreements with O.K." Pet. App. 24A n.14.

but of sales of inventory (Resp. Br. 3). In these circumstances, quite apart from any payments O.K. had made on the account, the amount of the lien was not specific and definite because Kimbell's claim was subject to a variety of defenses and uncertainties: the amount and composition of the inventory in fact delivered, the correctness and reasonableness of the price, the amount and value of defective or returnable items, the accuracy of the bookkeeping, and various other factors. The supplying of a wide variety of goods on open account through repeated deliveries over an extended period, as here, is very different, with respect to the definiteness of the amount owned, from loans of money evidenced by notes signed by the debtor and bearing face amounts.

The present case is analagous to the cases involving liens for attorneys fees, which this Court has held to be inchoate until reduced to judgment or set by a court. See *United States* v. *Pioneer American Insurance Co., supra,* 374 U.S. 84; cf. *United States* v. *Equitable Life Assurance Society,* 384 U.S. 323 (1966). There, as here, there is no advance agreement or evidence with respect to the amount owed. Services or goods are provided or supplied, and their value or price is recorded on the books of the provider or supplier, but the reasonableness of the amount charged is open to dispute, possibly on a number of grounds, by the person whose property is subject to

the lien.[18] In contrast, the signatory of a note such as those in *Crest Finance* is bound to repay the face amount of the note, absent fraud or other extraordinary circumstances. We therefore submit that respondent's lien was not analagous to the lien in *Crest Finance,* but was required to be reduced to judgment before it became choate; this did not occur until after the SBA-guaranteed loan was made and after the Bank's security interest was assigned to the SBA.

B. Finally, respondent and amicus argue (Resp. Br. 3–4; Amicus Br. 30–36) that the SBA's lien dates only from February 1971, when the SBA made good its 90% guaranty of the Bank's loan,[19] instead of from February 1969, when the Bank made the SBA-guaranteed loan and filed the financing statement securing it. This argument does not aid respondent because, for the reasons we have just outlined, respondent's lien did not become choate until it was reduced to judgment in February 1972.[20]

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[18] In *United States* v. *Pioneer American Insurance Co., supra,* the attorney had provided some services at the time the federal lien was filed; the final amount allowed by the state court "set the fee considerably below the sum requested." These unliquidated attorneys fees were held to be inchoate at the time the tax lien was filed.

[19] The Bank assigned its security interest to the SBA on December 30, 1970, and the assignment was filed on January 21, 1971 (see our main brief at 5–6).

[20] Amicus is therefore incorrect in asserting (Amicus Br. 30) that "SBA's claim in this case depends upon its assertion that the choateness of Kimbell's security interest must be measured as of February, 1969, when the Bank's security interest was perfected."

In addition, the SBA's interest is properly measured from the filing of the Bank's financing statement in February 1969. The court of appeals correctly so held (Pet. App. 26A), citing *United States* v. *Eklund*, 369 F. Supp. 1052, 1054–1055 (S.D. Ill. 1974).[21] Amicus relies (Br. 34–35) on cases construing the Bankruptcy Act and the insolvency statute (31 U.S.C. 191), including *United States* v. *Marxen*, 307 U.S. 200 (1939). In *Marxen*, this Court held that where the government guarantees a loan but accepts assignment of it only after the borrower becomes insolvent or bankrupt, the government is not entitled to its special bankruptcy priority or to its priority under 31 U.S.C. 191; instead, it takes only the priority to which the assignor was entitled.

Those cases, however, construe statutes that specifically require rights to be frozen as of the time of insolvency or bankruptcy. See *United States* v. *Marxen, supra*, 307 U.S. at 207; *United States* v. *Oklahoma*, 261 U.S. 253, 259–260 (1923). There is no comparable statutory requirement in this case. And equitable considerations favor dating of the government's lien from the date when the guaranteed security agreement is filed, since the government's obligation on the guarantee is fixed as of that date. Cf.

[21] Contrary to amicus's suggestion (Br. 33), the *Eklund* case did involve assignment to the SBA of an interest in a loan guarantee, in addition to direct participation in the loan by the SBA. The court accorded both SBA interests priority as of the dates of the original guarantee and the participation by the SBA. See 369 F. Supp. at 1054–1055.

United States v. *Summerlin*, 310 U.S. 414, 417 (1940).[22]

In any event, respondent should not be permitted to deny that the SBA's lien attached at the time the Bank's financing satement was filed, since respondent had actual notice of the SBA's role in guaranteeing the Bank's loan at the time the loan was made. See our main brief at 3–4, 52 n.58; App. 61–64.[23] In the Federal Tax Lien Act of 1966, even the limited priority that Congress gave to future advances made within 45 days after the filing of the tax lien is withheld if the "lender or purchaser had actual notice or knowledge of such tax lien filing." 26 U.S.C. 6323(c)(2)(A). Assuming that the policy of that Act has significance beyond the area of tax liens, the policy should be applied here to prevent respondent from taking priority over the SBA with respect to advances it made to O.K. after it had actual notice that the SBA was guaranteeing the secured loan from the Bank.

[22] In contrast, respondent was under no obligation to make the future advances that it did make subsequent to the Bank's loan.

[23] The court of appeals recognized that "Kimbell was aware of Republic's lien and—so the record suggests—the SBA's guaranty of the loan the lien secured" (Pet. App. 28A–29A; footnote omitted). Yet the court reasoned (*id.* at 29A) that under the Texas U.C.C., "this notice could not affect Kimbell's decision whether to advance funds because under state law its advances were secured by and took the priority of the 1966 and 1968 security agreements." This reasoning appears to beg the question whether the applicable rule on relation-back of future advances is the U.C.C. rule or the "actual notice" rule—a question the court expressly left open (Pet. App. 28A & n.18).

CONCLUSION

For the foregoing reasons and the reasons given in our main brief, the judgment of the court of appeals should be reversed.

Respectfully submitted.

WADE H. MCCREE, JR.,
Solicitor General.

JANUARY 1979.

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1978

No. 77-1359

UNITED STATES OF AMERICA,
Petitioner,

v.

KIMBELL FOODS, INC.,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR NATIONAL COMMERCIAL FINANCE CONFERENCE, INC. AS AMICUS CURIAE

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SUMMARY OF THE FACTS

This case involves a controversy over the priority of two ordinary security interests in equipment and inventory, both of which were duly perfected by filing under Article 9 of the Uniform Commercial Code (hereinafter "the U.C.C." or "the Code"). The first was granted to Kimbell Foods, Inc. ("Kimbell") and the other to Republic National Bank of Dallas ("Bank"). A ninety percent interest in the Bank's secured claim was eventually assigned to the Small Business Admin-

istration ("SBA"), and that secured claim is owned by both the Bank and the SBA. The debtor, O.K. Supermarkets, Inc. ("O.K."), was not alleged or proven to be insolvent at any time relevant to this case.

O.K. owned and operated a chain of supermarkets. Kimbell is a wholesale grocer which for several years sold grocery inventory to O.K. on a weekly basis. In November, 1968, to secure two promissory notes delivered by O.K. to Kimbell, O.K. executed and delivered to Kimbell a security agreement which granted to Kimbell a security interest in existing and after-acquired equipment and inventory at O.K.'s supermarkets. The security agreement provided by virtue of a standard future advance clause that the collateral also secured the repayment of subsequent liabilities arising from periodic sales of inventory on credit to O.K.[1] Interest and attorneys fees were also secured.

The security interest granted to Kimbell was duly perfected in November, 1968, by filing with the Secretary of State of Texas in accordance with the provisions of the Texas Uniform Commercial Code (App. 46–47). The filing included a copy of the security agreement, thereby making public all the terms of the secured arrangement, including the future advance clause. (App. 16–25). As of November, 1968, there were no other security interests in O.K.'s assets.

Three months later, in February, 1969, O.K. borrowed $300,000 from the Bank which was concurrently secured by a security interest in substantially the same coliateral previously given to Kimbell (App. 47–48). The Bank's security interest, granted under an ordinary security agreement, was

[1]The SBA took the position below that these liabilities were not intended to be within the scope of the future advance clause. The court ruled to the contrary, and the SBA has stated that this is not an issue before this Court. Petitioner's Brief at 8–9 n.11.

duly perfected by filing under the Texas Uniform Commercial Code on February 18, 1969 (App. 48). The SBA conducted its own appraisal of O.K.'s assets, and at the time of the loan guaranteed 90% of O.K.'s liability to the Bank (App. 48).

The Bank and the SBA were aware of the prior secured claim of Kimbell. On the date of the Bank loan, Kimbell's secured claim consisted of the unpaid balance on the notes and $18,390.93 for periodic inventory purchases covered by the future advance clause (App. 47). Proceeds of the Bank loan were used in part to pay the outstanding balance on O.K.'s notes to Kimbell, leaving the other indebtedness of $18,390.93 unpaid (App. 48).

No funds were advanced, directly or indirectly, by the SBA to O.K. The position of the SBA from the outset was that of an ordinary unsecured guarantor with a contingent liability to the Bank. No reference to the SBA guaranty appeared in the security agreement between O.K. and the Bank, and no financing statement or other filing at the time of the Bank loan mentioned the SBA (App. 67).

For almost two years after the Bank loan, Kimbell extended credit to O.K. on a weekly basis for sales of inventory in reliance upon its prior perfected security interest (App. 48). On January 15, 1971, Kimbell stopped selling to O.K. At that time the outstanding liability of O.K. to Kimbell was $18,258.57, substantially the same as it had been at the time of the Bank loan (App. 49). The amount of Kimbell's claim consisted simply of the amount of sales less payments received (App. 76–84). An action to recover this debt was filed by Kimbell on January 15, 1971 (App. 49).

On February 3, 1971, O.K. and the Bank agreed to a sale of collateral located at three of O.K.'s supermarkets, with the proceeds to be held in escrow pending resolution of the priority

of claims to the collateral represented by those proceeds. This agreement was approved by the SBA and Kimbell. The aggregate sale price of the collateral was $95,000.[2]

The SBA honored its guaranty and paid $252,331.93 to the Bank on February 3, 1971, which represented 90% of O.K.'s indebtedness to the Bank (App. 49–50). In consideration for this payment to the Bank, the SBA received an assignment of a 90% interest in the Bank's secured claim.[3] This was the first time that SBA funds were advanced in connection with the Bank's loan to O.K. Until that time the SBA was a contingent unsecured creditor.

Kimbell obtained a judgment in state court against O.K. on February 4, 1972, in the amount of $24,445.37 (App. 27–29). This represented the exact amount of O.K.'s principal debt to Kimbell, as reflected on the statements of account in January, 1971 ($18,258.57), plus interest ($1,186.80) and attorneys' fees ($5,000). This case arose when Kimbell brought the present suit in the United States District Court for the Northern District of Texas, seeking a declaration that its perfected security interest in the proceeds of its collateral held in escrow had priority over the claim of the Bank and the SBA (App. 8–15).

INTEREST OF AMICUS CURIAE IN THIS CASE

The National Commercial Finance Conference, Inc., *amicus curiae* in this case,[4] is a non-profit membership corporation organized under the laws of Delaware, with its principal office in New York. The Conference is the national trade association for the commercial finance and factoring industry, having almost one hundred and fifty members, including small enterprises and large publicly-held companies as well as nine of the ten largest banks in the United States or their subsidiaries.

[2]Of this amount, $38,000 was attributable to fixtures and equipment and $57,000 was attributable to inventory (App. 49–50).

[3]In anticipation of this action, on January 21, 1971, the SBA filed a form notice of assignment with the Texas Secretary of State under Article 9 of the U.C.C., thereby protecting the SBA from any possible action by the Bank which might release or amend the existing financing statement in the Bank's name. U.C.C. §9-405.

[4]This brief is filed pursuant to written consent of both parties to the case, in accordance with Rule 42 of the Court.

The heart of the commercial finance business is asset-based financing, including equipment leasing and factoring. The most common forms of collateral are inventory, accounts receivable, and equipment. Members of the Conference operate on a national, regional and local scale, extending secured credit to businesses, often through the financing of accounts receivable and inventory on a revolving basis. Most of these businesses are small and medium-sized enterprises, which depend upon the availability of secured financing for their existence and growth. For example, accounts receivable financing often enables a borrower to survive the growth or contraction periods in its business by providing funds prior to the maturity date of its receivables. Similarly, inventory financing allows a borrower to purchase inventory needed for cyclical or seasonal buildups or to supplement cash needs during periods of low volume.

The importance of the commercial finance industry to small business has long been recognized. Twenty years ago, the Board of Governors of the Federal Reserve System reported to Congress as follows:

> Commercial finance companies and factors play a significant role in the financing of small business in manufacturing and wholesale trade . . .
>
> Commercial financing and factoring are particularly significant in a study of small business financing because credit is made available to small businesses that do not have access to bank credit or to the markets for equity and long-term debt funds.

Federal Reserve System, Financing Small Business, Report to the Committees on Banking and Currency and the Select Committees on Small Business, 85th Cong., 2d Sess. 449–50 (Comm. Print 1958).

In response to the rapidly expanding needs of such borrowers, secured financing has grown dramatically and has become a significant part of the national credit market. The annual volume of financing by the commercial finance and factoring industry has increased from approximately $5,000,000,000 in 1950 to over $70,000,000,000 in 1977.

As businessmen, the members of the Conference expect to take risks on secured loans. They know that there is a danger of insolvency and sometimes fraud. They also know that their security interests will be inferior to earlier perfected liens and security interests. Secured lenders therefore review the appropriate public records to determine the relative priority of their security interests in the collateral. This review permits them to consider the highly competitive market price for their loans and services in light of the risks of asset-based financing. The borrowers with whom they will do business and the structure and amount of the secured transaction turn, in large measure, on the established expectations resulting from notoriety of liens and security interests in the public record.

Reliance on public filings has been aided by the widespread adoption of the Uniform Commercial Code, which has discouraged secret encumbrances while permitting flexible security devices designed to satisfy modern commercial needs. In only a decade, the Uniform Commercial Code has developed into a truly national law of commerce, having been adopted in 49 states, Puerto Rico, and the District of Columbia. It has provided uniformity and certainty which

have greatly facilitated and increased the availability of secured lending to small businesses for which credit otherwise is not available.

The government's position in this case is that a government agency can acquire a junior security interest and thereby make it senior. If this Court were to adopt that theory, a substantial risk would be added to the commercial financing industry in this country. A careful secured lender cannot reasonably predict whether the government might decide to provide secured credit, or even an unsecured secret guaranty, on some date following a private senior secured loan. Once the government's presence as a commercial lender is known, the government's position would require a lender providing revolving credit secured by accounts receivable or inventory to terminate financing and liquidate its collateral to preserve its priority position. In most cases, that is not possible without destroying the borrower's business, and in many instances it would also cause irreparable injury to the lender through a loss of the going concern value of its collateral. The economic result of the government's position would be to increase the cost of money to small and medium-sized businesses which are dependent on asset-based financing, and significantly reduce the availability of secured credit to those businesses.

SUMMARY OF ARGUMENT

This is a case of first impression which involves two principle issues. Both issues must be decided in the SBA's favor for it to achieve priority over Kimbell's earlier perfected security interest.

The first issue is whether the choate lien doctrine should be extended to decide the priority of two consensual security interests created pursuant to the Uniform Commercial Code,

outside of the context of the Federal Tax Lien Act and the insolvency priority statute. 26 U.S.C. § 6321 *et. seq.* (1976), 31 U.S.C. § 191 (1976). This issue apparently has never before been raised by the government in this or any other court, although the government's brief conveys the contrary impression. Even in the limited contexts in which the choateness doctrine has been applied, it has been heavily criticized and greatly restricted by Congress, particularly to the extent it has been applied to consensual liens or security interests.

Since the choate lien doctrine first appeared fifty years ago, a uniform body of law governing the priority of consensual security interests in personal property has been adopted nationwide—Article 9 of the Uniform Commercial Code. The federal courts have recognized that the U.C.C. provides the proper source from which to draw federal common law rules, particularly in cases concerning complex commercial security interests. It is to the Code, rather than to the choateness doctrine, that the federal courts should look to measure the adequacy and relative priority of consensual security interests. Reliance upon the U.C.C. would result in a priority system as between security interests which would provide fair, clear, and uniform rules for resolving priority disputes applicable to all parties, including the government.

The second issue, if this Court chooses to extend the choate lien test to the security interests in this case, is whether Kimbell's security interest satisfied that test at the relevant time. Kimbell's security interest was certain as to the identity of its holder, the amount of the debt, and the identity of the collateral as of January 15, 1971, prior to the time that the SBA advanced funds and acquired a 90% interest in the Bank's junior security interest. The government argues that Kimbell's security interest must meet the choateness test as of the time the Bank perfected its interest, in 1969. Both the case law and common sense dictate, however,

that the government cannot make the choateness test applicable retroactively simply by accepting an assignment of a privately-held security interest.

ARGUMENT

I.

THE CHOATE LIEN TEST IS NOT APPLICABLE TO KIMBELL'S PERFECTED SECURITY INTEREST.

This case involves the relative priority of two security interests created and perfected under Article 9 of the U.C.C.[5] Thus, the case is unlike any of the cases on which the government relies. There is no dispute that the Kimbell security interest was granted and perfected first and the Bank's security interest second under the U.C.C. The acquisition of an interest in the junior security interest by any party other than the government could not have affected or even raised a question about the established priority of the Kimbell security interest. The voluntary purchase by the SBA of a portion of the junior security interest did nothing but change the identity of the owner of that interest, long after the parties had relied on their respective positions in extending credit. As a result of this change of ownership, the SBA claims that its interest in the junior security interest now has priority over Kimbell's security interest. The basis of that claim is that Kimbell's security interest is "inchoate."

The Congress, courts and commentators have repeatedly recognized that the choateness doctrine has resulted in unfairness, confusion and uncertainty even in the limited categories of cases in which it has been applied, and the recent trend has been to narrow substantially or eliminate the doctrine. Nonetheless, the SBA now proposes to extend the

[5] TEX. BUS. & COM. CODE ANN. §§ 9.101 *et seq.* (Vernon). Both security interests were created and perfected in Texas.

choate lien test into an entirely new area, where it will serve no function other than to disrupt established commercial expectations of secured lenders, increase the volume of litigation in the federal courts, and unjustly enrich the government acting as a consensual creditor, providing it a windfall at the expense of other secured parties. Such an extension should not be permitted.

A. THERE IS NO STATUTORY OR JUDICIAL BASIS FOR EXTENDING THE CHOATE LIEN TEST TO DETERMINE THE PRIORITY OF TWO CONSENSUAL LIENS OR SECURITY INTERESTS.

The choate lien test has been considered by the courts and by the Congress in several contexts. The thrust of the government's brief is to suggest that the applicability of that test to this case has been previously established. This position is unsupported by any statute or case. Never before has the choate lien test been applied to a determination of the relative priority of two U.C.C. consensual security interests.

1. *The Statutory Framework*

Initially, it is important to recognize that the federal claim in this case does not fall within the scope of any federal statutes governing the priority of liens and security interests. Since no claim is made or evidence offered that O.K. was insolvent, the insolvency priority statute, R.S. § 3466,[6] does not apply. No federal tax lien is asserted, so that the provisions of the Federal Tax Lien Act[7] are not controlling, although the 1966 amendments thereto are useful to demonstrate the direction in which the choate lien doctrine has developed in recent years and the federal policy concerning the doctrine expressed by the Congress. Finally, this is not a bankruptcy proceeding,

[6]31 U.S.C. § 191 (1976).

[7]26 U.S.C. §§ 6321 *et seq.* (1976).

so that the priority provisions of Section 64 of the Bankruptcy Act[8] are not applicable.[9]

Nothing in the language or legislative history of the Small Business Act[10] suggests that Congress intended that the SBA should enjoy the superpriority which it claims here. While that Act is very specific in setting forth the rights and duties of the SBA, the only provision of the Act which deals with the priority of claims of the SBA subordinates such claims to certain state tax liens. 15 U.S.C. § 646 (1976). In testimony in 1958 before the Congressional subcommittee which was considering enactment of that subordination provision, the SBA acknowledged the priority of pre-existing liens without any reference to the possible applicability of the choateness doctrine to such interests:

> [t]he priority enjoyed by the United States under the provisions of title 31, United States Code, section 191, in the distribution of the *unencumbered* assets of any debtor of the United States who has become insolvent or who has made an assignment for the benefit of creditors . . . *is not applicable to property which is subject to a lien of any kind.*[11]

[8]11 U.S.C. § 104 (1976).

[9]If the SBA's security interest, acquired by assignment, had been a tax lien of which notice had been filed on the date SBA acquired a portion of the Bank's interest, it would have been junior to Kimbell's perfected security interest. As is discussed at p. 32 *infra*, a federal tax lien arises at the time of assessment but will not be valid as against perfected security interests until the time of filing. Unlike the tax lien example, the government here did not even have any claim until 1971.

Similarly, if bankruptcy had ensued, the SBA would simply have had a junior secured claim or an unsecured claim governed by Section 64 of the Bankruptcy Act, 11 U.S.C. § 104 (1976).

[10]15 U.S.C. §§ 631 *et seq.* (1976).

[11]Letter from Wendell B. Barnes, Administrator, Small Business Administration, in *Hearings before a Subcommittee of the Senate Committee on Banking and Currency, Credit Needs of Small Business*, 85th Cong., 2d Sess. 553–554 (1958) (emphasis added).

2. *Development of the Choate Lien Test*

The choate lien test is a judicially created and developed doctrine, although its scope has on occasion been limited by statute. The common law priority principle that "first in time is first in right" was recognized by this Court early in the history of American jurisprudence,[12] and has been adopted in this century as the "federal common law" rule determining the relative priority of lien claims of the United States.[13] *United States* v. *City of New Britain*, 347 U.S. 81 (1954). The choate lien doctrine arose prior to the development of the U.C.C.

[12] *Rankin* v. *Scott*, 25 U.S. (12 Wheat.) 177 (1827).

[13] The applicability of federal law to this case is not as clear as the government suggests at pages 16–17 of its brief. *See generally* Comment, *The Relative Priority of Small Business Administration Liens: An Unreasonable Extension of Federal Preference?*, 64 MICH. L. REV. 1107, 1124–1127 (1966). The portion of the security interest held by the government here was not "created in the course of exercising . . . constitutional functions", Petitioner's Brief at 17 n.14; it was a privately created security interest which later happened to be assigned to the SBA. The federal common law principle enunciated in *Clearfield Trust Co.* v. *United States*, 318 U.S. 363 (1943) does not require the application of federal law to every issue in every case to which the United States is a party. There are many circumstances under which the rights of the United States will be decided under state law rather than federal law. *See, e.g., United States* v. *Yazell*, 382 U.S. 341 (1966) (SBA subject to state coverture law); *Aquilino* v. *United States*, 363 U.S. 509 (1960) (state law determines whether taxpayer has rights in property to which a federal tax lien could attach); *United States* v. *Durham Lumber Co.*, 363 U.S. 522 (1960). The widespread enactment of the Uniform Commercial Code has substantially increased the desirability of adopting state law as the governing federal law on commercial law questions, and even the specific holding of *Clearfield Trust* may be far less compelling today than it was 35 years ago. Dunne, *Government Checks: A Leash for Leviathan?*, 95 BANKING L.J. 691 (1978). *See generally* 1A MOORE'S FEDERAL PRACTICE ¶ 0.321 at 3285 (2d ed. 1948).

Consequently, it might well be argued that state law should be applied to priority cases where the federal government acquires a security interest by assignment from a private party. *See United States* v. *Bryant*, 58 F. Supp. 663, 665 (S.D. Fla. 1945), *aff'd*, 157 F.2d

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as an adjunct[14] of the first in time principle, providing a standard in limited categories of cases for determining the date when a competing lien will be deemed to have arisen.

(a) Insolvency Priority Statute

The choateness doctrine first appeared in cases arising under the insolvency priority statute, R.S. § 3466. In spite of the sweeping language of that statute, enacted early in our nation's history,[15] that in certain kinds of insolvency proceedings "debts due the United States shall be first satisfied," courts had long held that R.S. § 3466 did not give the government priority over prior mortgages.[16] In the early twentieth

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767 (5th Cir. 1946) (state law governs where United States acquires negotiable instrument after maturity). Nevertheless, most lower courts have accepted the applicability of federal law in such cases as a matter of "dogma", without much analysis. 2 G. GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY 1054 n.10 (1965). *See, e.g., United States* v. *Eklund*, 369 F. Supp. 1052 (S.D. Ill. 1974). In order to address the critical questions concerning the choate lien test which are discussed herein, this Brief will assume that federal law applies.

[14] The government suggests that "some form of choateness requirement is a necessary complement to the first-in-time rule." Petitioner's Brief at 24 n.24. To the extent that this merely means that some method is required to determine when liens or security interests arise, the statement is neither controversial nor helpful. If it implies that the choate lien test is a logical and necessary consequence of the first-in-time rule, however, it is clearly incorrect.

[15] The predecessor to R.S. § 3466, 1 Stat. 512, 515, was enacted in 1797, using language substantially similar to that which is in force today. *See United States* v. *Moore*, 423 U.S. 70, 80–81 (1975); Kennedy, *From Spokane County to Vermont: The Campaign of the Federal Government Against the Inchoate Lien*, 50 IOWA L. REV. 724, 725 n.3 (1965). The concept of governmental priority has its origins in Magna Carta. W. PLUMB, FEDERAL TAX LIENS 191 (3d ed. 1972).

[16] *Conard* v. *Atlantic Ins. Co.*, 26 U.S. (1 Pet.) 386 (1828); *Brent* v. *Bank of Washington*, 35 U.S. (10 Pet.) 596 (1836). *See United States* v. *Texas*, 314 U.S. 480 (1941); *See generally* Kennedy, *The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien*, 63 YALE L.J. 905, 907–911 (1954), which contains an excellent discussion of the history of the choate lien test.

century, however, this Court began to formulate the principle that in order to defeat the government's statutory priority, a competing lien would have to satisfy a standard of certainty, or "choateness". *New York* v. *Maclay*, 288 U.S. 290 (1933); *United States* v. *Texas*, 314 U.S. 480 (1941); *United States* v. *Waddill, Holland & Flinn, Inc.*, 323 U.S. 1010 (1945); *United States* v. *Gilbert Associates, Inc.*, 345 U.S. 361 (1953). Thus, the choate lien doctrine developed as a limitation on a judicial exception to the literal meaning of the insolvency priority statute. The limitation, however, swallowed up the exception; since the beginning of the development of the choateness test, no lien or security interest has ever been found to be choate under the insolvency priority statute."

(b) Federal Tax Lien Act

The choateness concept was subsequently applied by this Court to determine the relative priority of federal tax liens

"Thus, at least in the insolvency context, the choate lien test has become a rule by which "the government always wins." *See* Petitioner's Brief at 42 n.48. Even the vitality of the venerable "mortgage" cases, *supra*, n.16, has been called into question under the modern reading of § 3466. *United States* v. *Texas*, 314 U.S. 480, 486 (1941); *New York* v. *Maclay*, 288 U.S. 290 (1933); 2 G. GILMORE, SECURITY INTERESTS in PERSONAL PROPERTY 1073 n.3 (1965). There is a growing belief that R.S. § 3466 has become a statutory anachronism, reflecting an outdated approach to the collection of government revenues which developed at a point in history when almost all government claims were tax claims. *See, e.g., H. B. Agsten & Sons, Inc.* v. *Huntington Trust & Sav. Bank*, 388 F.2d 156, 161–62 (4th Cir. 1967) (Haynsworth, J., concurring), *cert. denied*, 390 U.S. 1025 (1968). Reform of the insolvency priority statute along the lines of the 1966 Federal Tax Lien Act was deferred only because it would have complicated the legislative process in view of the overlapping jurisdictions of Congressional committees. *See* Plumb, *Federal Liens and Priorities—Agenda for the Next Decade*, 77 YALE L.J. 228, 293 (1967). While reform of the insolvency priority statute must be left to Congress rather than the courts, reliance upon that statute, rather than the 1966 Federal Tax Lien Act, as a source of federal policy concerning the choateness doctrine would be clearly misplaced.

and state statutory liens, outside the context of R.S. § 3466. *United States* v. *Security Trust & Savings Bank* 340 U.S. 47 (1950); *United States v. City of New Britain*, 347 U.S. 81 (1954). In several cases, the justification for the choateness requirement was set forth: the rule was designed to prevent state statutes from giving statutory liens which protect various kinds of special interests" a "superpriority" by dating them, for the purposes of the first in time rule, at an artificially early point in time. Thus, in *United States* v. *City of New Britain*, 347 U.S. at 86, this Court expressed concern that "a State could affect the standing of federal liens, contrary to the established doctrine, simply by causing an inchoate lien to attach at some arbitrary time even before the amount of the tax, assessment, etc., is determined."

The choate lien test, as developed in earlier cases and enunciated in *City of New Britain*, 347 U.S. at 84, is three-fold: in order for a lien to be choate, the amount due, the identity of the lienor, and the identity of the property subject to the lien must be certain. In the tax lien area, the doctrine was applied for the first time to a pre-U.C.C. consensual lien on personal property in *United States* v. *R. F. Ball Construction Co.*, 355 U.S. 587 (1958) (*per curiam*). No funds had been disbursed in *Ball* at the time notice of the tax lien was filed, which caused this Court to hold the consensual lien to be inchoate. Later, this Court recognized that a consensual lien is capable of satisfying the choateness test without the amount of the debt being reduced to judgment. *Crest Finance Co.* v. *United States*, 368 U.S. 347 (1961) (*per curiam*).

That the choateness doctrine has not been well understood is demonstrated in part by the fact that a great many of this

"The most common kinds of statutory liens to be involved in such cases have been those for state and local taxes and amounts owed to mechanics and materialmen. *See generally* Kennedy, *The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien*, 63 YALE L.J. 905 (1954).

Court's decisions concerning the doctrine have been reversals of lower court decisions. *See, e.g., United States* v. *Pioneer American Insurance Co.*, 374 U.S. 84 (1963); *Crest Finance Co.* v. *United States*, 368 U.S. 347 (1961) (*per curiam*); *United States* v. *R. F. Ball Construction Co.*, 355 U.S. 587 (1958) (*per curiam*); *United States* v. *Vorreiter*, 355 U.S. 15 (1957) (*per curiam*); *United States* v. *Colotta*, 350 U.S. 808 (1955) (*per curiam*).[19] Another measure of the uncertainty associated with the doctrine is the fact that this court has had to decide approximately 20 cases directly relating to the choateness doctrine in the past 50 years, and has denied certiorari in many others. Furthermore, the choate lien doctrine has attracted considerable scholarly criticism, while finding few defenders. *See, e.g.*, 2 G. Gilmore, *Security Interests in Personal Property*, 1052–1073 (1965); Plumb, *Federal Liens and Priorities—Agenda for the Next Decade*, 77 Yale L.J. 228 (1967); Kennedy, *From Spokane County to Vermont: The Campaign of the Federal Government Against the Inchoate Lien*, 50 Iowa L. Rev. 755 (1965); Kennedy, *The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien*, 63 Yale L.J. 906 (1954); Comment, *The Relative Priority of Small Business Administration Liens: An Unreasonable Extension of Federal Preference?*, 64 Mich L. Rev. 1107 (1966).

Prior to 1966, the choate lien test had been applied to only a few government consensual liens, none of which arose under the U.C.C. The Court had considered the choateness doctrine under the Tax Lien Act in only three consensual lien contexts: a series of loans secured by assignments of

[19]Professor Gilmore has compared the development of the choate lien test in the lower courts to a "parlor game in which all the players but one try to guess what the remaining player is thinking of", and has observed that the lower courts have had a singular lack of success in discerning the scope and meaning of the choateness doctrine. 2 G. Gilmore, Security Interests In Personal Property 1062 (1965).

accounts receivable (*Crest Finance*), a contingent commitment by a surety company (*Ball Construction*), and attorneys' fees for enforcing a mortgage which were unliquidated in amount until after the notice of tax lien was filed (*Pioneer American Insurance*). The rapid national adoption of the U.C.C., at a time when there was general dissatisfaction with the choate lien doctrine as applied in tax lien cases, led to the Federal Tax Lien Act of 1966,[20] under which the applicability of the choate lien doctrine to tax lien cases was greatly restricted, particularly with respect to security interests perfected under the U.C.C. Congressional dissatisfaction with the choateness doctrine, as applied to security interests, was evidenced by the fact that perfected security interests covering future advances, after acquired property, commitments to make future advances, and attorneys' fees received explicit protection in the 1966 amendments.[21]

The effect of the 1966 amendments was to limit dramatically the application of the choateness doctrine in the only area in which it had been applied by this Court at that time outside the insolvency priority statute. The relative priority of federal tax liens and security interests can now be resolved under the specific terms of the Act, without reference to the choate lien test. One of the major federal policies underlying the 1966 amendments was to harmonize the Tax Lien Act with the provisions of the U.C.C., to prevent or curtail the impairment of modern commercial financing transactions. S. Rep. No. 1708, 89th Cong., 2d Sess., reprinted in [1966] U.S. Code Cong. & Ad. News 3722; *Pine Builders* v. *United States*, 413 F. Supp. 77, 81 (E. D. Va. 1976); R. Henson, *Secured Transactions Under the Uniform Commercial Code* 105 (1973).

[20]Pub. L. No. 89-719, 80 Stat. 1125 (1966).

[21]26 U.S.C. §§ 6323(c)(2), (c)(4), (d) and (e) (1976).

(c) Consensual Liens and Security Interests Held by the Government

Despite continuing scholarly criticism and Congressional action aimed at limiting the scope of the choate lien test, some federal agencies, including the SBA, have become increasingly aggressive in their attempts to extend the doctrine into new areas.[22] In particular, those agencies have urged that the choateness doctrine should be extended beyond the scope of the tax lien and insolvency statutes to priority contests between consensual liens and security interests held by the government and competing statutory liens. This argument has taken on growing significance as the size and number of federal programs under which agencies of the United States acquire such voluntary commercial consensual liens and security interests has increased dramatically.[23]

Several federal courts of appeals accepted the government's position that the choate lien test should be used in cases in which the government holds a mortgage or security interest to determine the priority of various kinds of statutory liens.[24] Each of these cases, however, is entirely different from

[22] *See* Comment, *The Relative Priority of Small Business Administration Liens: An Unreasonable Extension of Federal Preference?*, 64 MICH. L. REV. 1107 (1966).

[23] The government stated in its Petition for Certiorari, at page 6, that the SBA alone now has approximately 3,400 cases in litigation at any given time, many of them involving priority questions. The most recent update to the Office of Management and Budget's CATALOG OF FEDERAL DOMESTIC ASSISTANCE indicates that there are now 1,044 federal assistance programs of various kinds, administered by 55 federal governmental agencies.

[24] *Chicago Title Ins. Co.* v. *Sherred Village Associates*, 568 F.2d 217 (1st Cir. 1978), *petition for cert. pending sub nom. Hercoform Inc.* v. *Chicago Title Ins. Co.* (No. 77-1611); *Willow Creek Lumber Co.* v. *Porter County Plumbing & Heating, Inc.*, 572 F.2d 588 (7th Cir. 1978); *United States* v. *General Douglas MacArthur Senior Village, Inc.*, 470

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this case. In these cases, the result generally would have been identical under the federal first in time rule even without the application of the choateness doctrine, since the federal mortgage was perfected prior to the filing of notice of the statutory lien.[25] More significantly, however, none of these cases relied upon by the government involved a competing mortgage or perfected security interest created under Article 9 of the U.C.C.; instead, all of them involved competing statutory liens, arising under a myriad of state statutes which provided for the priority of those liens in a variety of different manners, often regardless of the time when notice of the lien was filed or when the amount of the debt secured by the lien became liquidated and certain.[26]

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F.2d 675 (2d Cir. 1972), *cert. denied sub nom. County of Nassau* v. *United States*, 412 U.S. 922 (1973); *United States* v. *Oswald & Hess Co.*, 345 F.2d 886 (3d Cir. 1965); *United States* v. *County of Iowa*, 295 F.2d 257 (7th Cir. 1961); *Southwest Engine Co.* v. *United States*, 275 F.2d 106 (10th Cir. 1960); *United States* v. *Latrobe Constr. Co.*, 246 F.2d 357 (8th Cir.), *cert. denied*, 355 U.S. 890 (1957). Two circuits have disagreed. *United States* v. *Crittenden*, 563 F.2d 678 (5th Cir. 1977), *cert. granted*, 47 U.S.L.W. 3191 (U.S. Oct. 2, 1970) (No. 77-1644); *United States* v. *California-Oregon Plywood, Inc.*, 527 F.2d 687 (9th Cir. 1975); *Ault* v. *Harris*, 317 F. Supp. 373 (D. Alas.), *aff'd*, *Ault* v. *United States*, 432 F.2d 441 (9th Cir. 1970).

[25] *See, e.g., Chicago Title Ins. Co.* v. *Sherred Village Associates*, 568 F.2d 217 (1st Cir. 1978), *petition for cert. pending sub nom. Hercoform, Inc.* v. *Chicago Title Ins. Co.* (No. 77-1611); *Willow Creek Lumber Co.* v. *Porter County Plumbing & Heating*, 572 F.2d 588 (7th Cir. 1978); *United States* v. *General Douglas MacArthur Senior Village, Inc.*, 470 F.2d 675 (2d Cir. 1972), *cert. denied sub nom. County of Nassau* v. *United States*, 412 U.S. 922 (1973); *United States* v. *County of Iowa*, 295 F.2d 257 (7th Cir. 1961); *Southwest Engine Co.* v. *United States*, 275 F.2d 106 (10th Cir. 1960).

[26] In light of the intense scholarly and judicial criticism of the judicially-created choate lien test, *see supra* at pp. 15–16, the steps taken by Congress to limit the doctrine, *see* 26 U.S.C. § 6323 (1976), 15 U.S.C § 646 (1976), and the fact that this Court has never applied the test except under the insolvency and tax lien statutes, a

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Even in those circuits in which the choateness test has been extended for the benefit of the United States as holder of a commercial mortgage lien to defeat statutory liens, that extension has been accompanied by reluctance and considerable critical commentary. For example, in *Chicago Title Insurance Co.* v. *Sherred Village Associates*, 568 F.2d 217, 221 (1st Cir. 1978), *petition for cert. pending sub nom. Hercoform, Inc.* v. *Chicago Title Ins. Co.* (No. 77-1611), which is quoted in part in Petitioner's Brief at page 46, the Court of Appeals for the First Circuit discussed the undesirability of the choateness doctrine even in the more traditional statutory lien area:

> Choateness has proven a fatal handicap in the race between a mechanic's lienor and a federal lienor. It appears to serve no strong policy, since the federal lienor stands to be enriched by the increase in the property value caused by the work of the mechanic's lienor, while the latter stands without remedy. Moreover, this built-in advantage is not necessary to protect the federal investment; the government in mortgage lending and insuring may choose its debtors and set its terms.

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compelling argument could be made that many of these cases are incorrectly decided or are no longer controlling. *See United States* v. *Crittenden*, 563 F.2d 678 (5th Cir. 1977), *cert. granted* 47 U.S.L.W. 3191 (U.S. Oct. 2, 1978) (No. 77-1644); *Ault* v. *Harris*, 317 F. Supp. 373 (D. Alas.), *aff'd, Ault* v. *United States*, 432 F.2d 441 (9th Cir. 1970). The government itself recognizes that this case is distinguishable from those involving state lien superpriorities. At several points in its certiorari petition in the *Crittenden* case, the government acknowledged that it would be possible for it to lose this case but prevail in *Crittenden*. Petition for Writ of Certiorari at 7, 9, *United States* v. *Crittenden* (No. 77-1644). While there may be substantial justification for this approach to statutory liens, it involves an issue which is raised in *Crittenden* and *Hercoform* v. *Chicago Title Ins. Co.* (No. 77-1611) but which is not present here. Accordingly, the National Commercial Finance Conference takes no position in this brief concerning the appropriate resolution of that question.

That court went on to conclude that it was unwilling to try to develop an alternative to the choateness test in the circumstances of that case. In so doing, however, the First Circuit expressly distinguished this case, acknowledging that the Fifth Circuit's adoption of the U.C.C. "*fitted the case admirably*, since the U.C.C. is of general, nationwide application, with no quixotic parochial variations."[27] 568 F.2d at 222 (emphasis added).

Viewed in a historical perspective, the significance of the government's assertions in this case becomes apparent. The choate lien doctrine arose in conjunction with a judicial exception to a federal priority statute which on its face appeared to be absolute. That exception, however, has been applied in such a way that it has ceased to perform any mitigating function. The choateness concept was then imported into the Tax Lien Act, but its application there was subsequently severely limited by the 1966 Federal Tax Lien Act. Thereafter, the concept was revived by government agencies in some lower courts to defeat special interest state statutory liens creating superpriorities competing with the rapidly growing number of federal consensual security interests and mortgage liens.

Now, however, apparently for the first time, and despite the fact that a uniform priority system for consensual security interests has been adopted throughout this country (except in Louisiana) in the form of Article 9 of the U.C.C., the SBA seeks to extend the choateness doctrine to a priority contest between two ordinary consensual security interests. That proposed extension of the doctrine would serve only to enrich the federal Treasury at the expense of private secured

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[27] A similar statement was made in the Brief in Opposition of the non-federal respondents before this Court in *Hercoform*. Brief for Chicago Title Insurance Co. and New England Merchants National Bank in Opposition at 7-8, *Hercoform* v. *Chicago Title Ins. Co.* (No. 77-1611).

creditors, while creating uncertainty and confusion in an area of commerce in which stability and certainty concerning the legal effect of contracts are essential. Consequently, the Conference urges this Court to reject this attempt by the SBA to expand the scope of the choate lien doctrine into the field of consensual security interests, where the government acts as a voluntary commercial lender, not a sovereign taxing authority.

B. PERFECTION UNDER THE UNIFORM COMMERCIAL CODE IS THE PROPER BASIS FOR DETERMINING WHICH SECURITY INTEREST WAS FIRST IN TIME UNDER FEDERAL PRIORITY LAW.

Article 9 of the Uniform Commercial Code has been adopted with minor variations by the legislatures of 49 states and Puerto Rico and by the Congress for the District of Columbia.[28] It provides a well thought out, coherent and comprehensive system for the creation, perfection and enforcement of virtually all security interests, and for determining their relative priority.[29] It was to those provisions, rather than to the choate lien doctrine, that the court of appeals properly turned as the source of federal priority law in this case.

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[28]The undesirability of extending the choateness doctrine to this kind of case is highlighted by Congress' adoption of the U.C.C. for the District of Columbia. The federal common law, of which the choateness doctrine is a part, operates only where there is no superseding federal statutory rule, such as the Federal Tax Lien Act or the Bankruptcy Act. The underlying logic of the choateness doctrine is that the various states should not be allowed to interfere with federal rights through the enactment of state superpriority statutes. Thus, the choateness doctrine has no applicability in the District of Columbia, where the Congress legislates. If the SBA is successful in this case, the choateness doctrine will apparently apply to cases such as this throughout the country *except* in the District of Columbia. The lack of logic in this disparity is readily apparent.

[29]*See particularly* U.C.C. §§ 9-303, 9-312.

Since the creation of the U.C.C., and particularly after its widespread acceptance throughout the United States, the federal courts have repeatedly looked to the Code as an authoritative source of federal common law in cases to which the United States is a party. *See, e.g., United States* v. *Hext*, 444 F.2d 804 (5th Cir. 1971); *United States* v. *Wegematic Corp.*, 360 F.2d 674 (2d Cir. 1966); *In re Yale Express System, Inc.*, 370 F.2d 433 (2d Cir. 1966); *Bumb* v. *United States*, 276 F.2d 729 (9th Cir. 1960); *Matter of Ocean Electronics Corp.*, 451 F. Supp. 511 (S.D. Cal. 1978); *United States* v. *Topeka Livestock Auction, Inc.*, 392 F. Supp. 944 (N.D. Ind. 1975).[30] As Judge Friendly observed in *United States* v. *Wegematic Corp.*, 360 F.2d at 676 (emphasis added):

> When the states have gone so far in achieving the desirable goal of a uniform law governing commercial transactions, it would be a distinct disservice to insist on a different one for the segment of commerce, important but still small in relation to the total, consisting of transactions with the United States.

Article 9 of the Code has been relied upon particularly frequently as the source of the "federal law merchant" concerning security interests.[31] The provisions of the Code provide a fair and simple method for determining the validity and priority of security interests which is well understood by the courts and relied upon in the commercial world. Since the underlying priority principle of the Code is the "first in time" rule applied under the federal common law,[32] it is en-

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[30]See also 1A MOORE'S FEDERAL PRACTICE ¶ 0.321 at 3285 (2d ed. 1948).

[31]*See, e.g., United States* v. *Hext*, 444 F.2d 804 (5th Cir. 1971); *In Re Yale Express System, Inc.*, 370 F.2d 433 (2d Cir. 1966); *Matter of Ocean Electronics Corp.*, 451 F. Supp. 511 (S.D. Cal. 1978); *United States* v. *Topeka Livestock Auction, Inc.*, 392 F. Supp. 944 (N.D. Ind. 1975).

[32]The Code contains a few carefully delineated exceptions to the pure first in time rule, relating to such matters as purchase money

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tirely consistent that this Court apply the Code provisions governing the time when security interests such as are involved in this case, whether held by the government or others, are perfected for the purpose of determining their relative priority under the federal rule.

The government complains in its brief that the opinion of the court of appeals in this case leaves some unresolved questions, since it adopts one aspect of the Code to resolve the question in this case, but does not specify what the source of federal law will be for any other priority questions which may arise. This hardly seems a significant problem, particularly when compared to the uncertainty and case-by-case development of common law rules by the federal courts which would necessarily result from an extension of the choateness test. To the extent that this question is considered at this time, however, the Conference believes that established commercial expectations would be best served by complete reliance upon the perfection and priority rules of Article 9, which is based almost entirely on the first in time principle.

The fact that some states may have a few nonuniform Code provisions does not affect the essential uniformity and desirability of using the Code to determine priority. *See* Petitioner's Brief at 50–51 n.56. The possibility of some minor nonuniformity in language or interpretation exists with respect to any part of the Code, but this contingency has done nothing to deter the federal courts from relying upon the Code as a basic source of federal common law rules and, if necessary, following the weight of authority in the rare in-

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security interests and perfection by possession. The existence of those exceptions, however, does not affect the basic comparability of the Code and common law priority rules. The government itself may choose, for example, to perfect by possession (pledges of securities) or finance the acquisition of equipment or inventory under purchase money security interests to attain priority over other secured parties.

stances of nonuniformity. *See, e.g., United States* v. *Burnette-Carter Co.*, 575 F.2d 587 (6th Cir. 1978), *petition for cert. pending* (No. 78-257)[33]; United States v. *Hext*, 444 F.2d 804, 811 (2d Cir. 1971). To the extent that such instances ever arise, they may provide the federal courts with the opportunity to rely upon a clear general set of rules while allowing for flexibility with respect to specific details on which there may be public policy differences in some states.

By looking to the Code to determine which security interest is first in time, this Court will be applying a rule which has been interpreted, explained, and refined by a comprehensive body of precedent, a substantial portion of which has developed in the federal courts. This will lead to a consistency of result which will reduce the need for litigation involving a case-by-case determination of federal priority rules in the area of secured financing, and will help to foster secured lending pursuant to a set of rules that everyone, including the government, understands and relies upon. By contrast, expansion of the choate lien doctrine to cover security interests competing with those held by the government as a voluntary commercial lender will require a prolonged, uncertain, case-by-case consideration by the federal courts of the exact content of the rule in this new context.[34] To exactly what cases will the

[33]In the *Burnette-Carter* case, the application of Article 9 of the U.C.C. as federal common law resulted in a decision in favor of the United States. This was also true in *Matter of Ocean Electronics Corp.*, 451 F. Supp. 511 (2d Cir. 1966).

[34]One issue which may arise, regardless of whether the choateness rule is applied here, is the circuity problem. That problem exists when under applicable law each of three liens or security interests is superior to one of the other two, but junior to the third. Such circuity is the result of superimposing one priority system on top of another. W. PLUMB, FEDERAL TAX LIENS 117 (3d ed. 1972). There is no one perfect solution to this problem, but the one considered most fair was adopted by Congress when it revised Section 67c of the Bankruptcy Act. 11 U.S.C. § 107 (1976); *see generally* 4 COLLIER ON BANKRUPTCY ¶ 67.27 (14th ed. 1940).

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doctrine be extended?[35] What standard of choateness will be applied?[36] These and other questions, many of which probably cannot be anticipated at this time, would have to be addressed by the district courts, the courts of appeals, and this Court if the choateness doctrine is extended to this case.

Another reason for rejecting the government's position in this case is the bizarre consequence of its application. In cases such as this where the SBA acquires only a partial assignment of a claim, the federal courts will be confronted with the anomaly of a single secured claim which has two different priorities: a first priority for the federally-owned portion, but a third priority for the other portion retained by the private assignor, which is junior to the competing perfected security interest under the Code.

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If this Court affirms the Fifth Circuit's decision in *United States* v. *Crittenden* (No. 77-1644), the circuity problem will be substantially resolved, since the result will be a relatively uniform priority system when the government holds a security interest, even for competing statutory mechanic's liens.

[35]Another question, for example, would be whether the doctrine should be applied in the District of Columbia. *See* p. 22 n.28, *supra*. The applicability of the doctrine to the priority of consensual liens and security interests arising under the federal statutes would also be open to question. *See, e.g.* Federal Ship Mortgage Act, 46 U.S.C. § 911 *et seq.* (1976); Federal Aviation Act of 1958, § 503, 49 U.S.C. § 1403(a)(2) (1976). *See generally* 1 G. GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY 401-61 (1965). These are only a few examples of the uncertainties inherent in the government's position, which demonstrate that the problem is not exclusively one of state law.

[36]*Cf. United States* v. *Vermont*, 377 U.S. 351, 357 (1964) (different standards of choateness applicable under insolvency and tax statutes); *Kimbell Foods, Inc.* v. *Republic Nat'l Bank*, 557 F.2d 491, 502 n.14 (5th Cir. 1977) ("the same reasons that argue against the extension of the choateness doctrine to federal contractual liens would urge us to adopt a less stringent standard of choateness in this context.").

In its brief, the government suggests that application of the choateness doctrine is necessary to uphold "the expected stability of decision." Petitioner's Brief at 39. In fact, the opposite result is mandated by that principle. So far as the Conference is aware, except in cases governed by the insolvency priority statute, the SBA and other federal agencies have never before in this or any other court challenged the priority of Article 9 security interests perfected prior to security interests held by the government. Before this case arose, the commercial finance industry gave little consideration to the prospect that a government lender or guarantor could upset a pre-existing set of priorities of consensual security interests created pursuant to the U.C.C. by use of the choate lien test, particularly when the government relied on the Code to create and perfect its interest. Far from reflecting "expected stability of decision", the position taken by the government represents a significant departure from both past government practice and the existing expectations of private secured lenders. One commentator has characterized the District Court's decision in favor of the SBA in this case as "startling", observing: "This decision raises a frightening specter of federal power and demonstrates the wisdom of applying state law where rights have been fixed and relied upon in structuring contractual relationships." Burke, *Secured Transactions, Uniform Commercial Code Annual Survey*, 31 Bus. Law. 1583, 1586-87 (1976).[37]

The government's brief devotes considerable attention to the need for certainty in matters of commercial law. The Conference, as a trade association of businesses which must understand and consider security priority questions on a daily basis, is in wholehearted agreement with this objective.

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[37]*See also* Burke, *Secured Transactions, Uniform Commercial Code Annual Survey*, 33 BUS. LAW. 1931, 1936-37 (1978), commenting favorably on the court of appeals' opinon in this case.

The Conference believes, however, that the goal of commercial certainty will be subverted rather than achieved by expansion of the choateness doctrine to resolve priority questions between competing security interests arising under the Code.

Lenders in the secured financing business rely heavily on their ability to evaluate the priority of their security interests. That priority will usually determine whether credit will be extended, as well as on what terms. It is therefore essential to secured lenders and borrowers alike that the law governing priorities be definite, clear, and consistent. This essential certainty would be completely undermined by a rule under which a lender enters into a secured credit arrangement relying upon the knowledge that its security interest has priority under the Code, only to find that a federal agency voluntarily provided an unsecured guaranty of another loan years later, thereby completely rearranging the priorities to transform what would otherwise have been a senior interest into a junior one. This is exactly the sort of retroactive "bootstrapping" which is at the heart of SBA's argument.

The SBA as a voluntary commercial lender or guarantor is in as good a position as any other commercial lender to evaluate the risks associated with a particular loan. Many of the loans made or guaranteed by the SBA may entail more risk than those made by private lenders, because of the statutory restriction on the SBA to provide financial assistance only to the extent that it "is not otherwise available on reasonable terms from non-federal sources,"[38] but the SBA is also expressly directed to obtain adequate security for such loans.[39] Congress clearly intended that the SBA loan program

[38]15 U.S.C. § 636(a)(1) (1976).

[39]15 U.S.C. § 636(a)(7) (1976).

not disrupt the existing credit market.[40] There is no reason why, in choosing to make such loans, the SBA as a voluntary commercial lender should be able to take advantage of a special rule to achieve priority which would be unavailable to any other lender. As Mr. Justice Holmes has stated in another context, "The United States does business on business terms." *United States* v. *National Exchange Bank*, 270 U.S. 521, 534 (1926).

To the extent that the choateness rule is expanded to allow the SBA to defeat secured lenders with prior perfected security interests, every dollar returned to the SBA's "revolving fund" (Petitioner's Brief at 23) will be one less dollar available in the private credit market. There is not a single equitable consideration which warrants that result. Application of the choateness rule in that context would tend to replace private lenders with a public one.

There may be some logic to protecting the government from a myriad of state statutes exalting various kinds of special interest liens retroactively to superpriority status, particularly where the government is unable to take advantage of such provisions on equal terms.[41] There is, however, no justification in the absence of Congressional authorization for immunizing government commercial lending agencies from the rules of nationwide applicability embodied in the U.C.C., of which they can take advantage on the same basis

[40]In its opinion in this case, the court of appeals noted that extension of the choate lien doctrine to this case would be inconsistent with the policy of the Act to strengthen small businesses. *Kimbell Foods, Inc.* v. *Republic Nat'l Bank*, 557 F.2d 491, 500 (5th Cir. 1977).

[41]This is the question presented in *Crittenden* and *Hercoform*. As has been stated above, *supra* n.26, those cases are very different from this one, and the Conference takes no position on them, other than to point out that even in that context the choate lien doctrine has been the subject of substantial criticism. *See supra*, pp. 15–21.

as any other secured lender. The U.C.C. places all voluntary secured lenders, including agencies of the government, on an equal footing and in a position to rely on the notoriety of security interests in the public record.

II.
THE PERFECTED SECURITY INTEREST OF KIMBELL WAS CHOATE AND FIRST IN TIME.

The Conference believes that the proper basis for affirmance in this case is that the choate lien test is not applicable to this transaction. For the SBA to achieve priority in this case, however, it must do more than extend the choate lien test to this non-insolvency, non-tax lien priority contest. To prevail, the SBA must also establish that it can acquire a junior security interest from private lender and thereby make it senior, with priority over a perfected security interest that was fully choate at the time of the assignment. That proposition is unsupportable both in law and in logic, and if adopted would destroy any semblance of order and certainty which might survive the SBA's proposed extension of the choate lien test.

A. FOR THE PURPOSE OF APPLYING THE CHOATE LIEN TEST, THE SBA OBTAINED ITS SECURITY INTEREST ON THE DATE IT FIRST ADVANCED FUNDS AND ACQUIRED AN INTEREST IN A SECURED CLAIM.

The function of the choate lien doctrine has always been to test the certainty of a competing lien or security interest at the time that the federal government acquires its lien or security interest. The SBA's claim in this case depends upon its assertion that the choateness of Kimbell's security interest must be measured as of February, 1969, when the Bank's security interest was perfected. That contention, however, is contrary to both existing authority and common sense.

It is uncontroverted that the SBA did not have a security interest in O.K.'s property in February, 1969, or at any time prior to February 3, 1971, when it acquired part of the Bank's secured claim. The SBA conceded this at oral argument in the court below. 557 F.2d at 505. Nonetheless, the SBA contends that its security interest "attached"[42] in 1969. Prior to February 3, 1971, however, when the SBA honored its guaranty, the SBA had at best an unsecured contingent claim, while the Bank held the entire junior security interest. Consequently, the SBA is claiming that a requirement which is designed to protect security interests and liens of the federal government should be applied retroactively, as of a date when the United States did not possess any security interest or lien and had not advanced any funds.

The Conference agrees that the SBA's assigned interest "relates back" to 1969 under state law, just as it would for any other assignee who acquires the interest of the assignor, subject to all of its limitations. If the Bank's security interest had been perfected in 1965, for example, it would not have lost its first in time priority as a result of the assignment to

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[42]The use of the concept of attachment in this context (by the government and by some courts) has contributed to the confusion associated with the choate lien doctrine. The government here obviously intends attachment to mean that the security interest which it has was sufficiently complete and effective to be valid for the purpose of applying the first in time rule and the choateness doctrine. The SBA does not describe, however, what is necessary for such attachment to occur.

The more common meaning of attachment is the point at which a security interest becomes enforceable against the debtor. Under the U.C.C., this generally occurs when (a) the debtor has signed a security agreement, (b) value has been given, and (c) the debtor has rights in the collateral. U.C.C. § 9-203. In order to take priority over other security interests, however, "perfection" (usually by filing a financing statement) is also required. U.C.C. § 9-312. Under the Code, it is perfection rather than attachment which determines the relative priority of security interests.

the SBA. That is something very different from relating back the applicability of the choateness doctrine. The assignment to the SBA did not damage the priority position of the Bank's security interest; the government, however, is attempting to use the assignment to *improve* the priority of 90% of that interest, by having the applicability of the federal choateness rule relate back. This is in complete contravention of the basic principle that an assignee acquires no better rights than those which are held by its assignor.

The sort of retroactive application of the choateness doctrine which is urged here by the government has never been permitted in the analogous situation in the federal tax lien area. Such a lien arises automatically at the moment the tax is assessed, 26 U.S.C. § 6322 (1976), which involves nothing more than an entry in government records. The lien is not valid against other perfected consensual liens or security interests, however, until notice of the tax lien is filed. 26 U.S.C. § 6323(a) (1976); *United States* v. *Pioneer American Insurance Co.*, 374 U.S. 84, 88 (1963). Thus, even prior to the restriction of the choate lien test by the Federal Tax Lien Act of 1966, choateness was tested as of the date when notice of the federal lien appeared in the public record. The choateness requirement did not relate back to the date of assessment, despite the fact that a federal lien arises at that time. The notions of reasonable reliance and established expectations which underlay that result in the tax lien area are equally applicable here.

Few courts have addressed this issue directly, but the case law which does exist indicates that the SBA cannot achieve an application of the choateness requirement at a point in time when no federal security interest or lien existed. The opinion of the court of appeals in this case does state that the SBA's security interest "attached" in 1969, 557 F.2d at 503, but it does so only after deciding that the choateness doctrine is inapplicable to this case. Consequently, the Fifth

Circuit did not in any sense sanction the retroactive application of that doctrine to this transaction.

The two cases cited by the government on this subject, *Small Business Administration* v. *McClellan*, 364 U.S. 446 (1960), and *United States* v. *Eklund*, 369 F. Supp. 1052 (S.D. Ill. 1974), do not support a contrary conclusion. In *McClellan*, a bankruptcy case involving the insolvency priority statute, the note held by the SBA was assigned to it after the filing of the petition in bankruptcy. The Court concluded that for the purposes of the insolvency priority statute, there was a "debt due the United States" as of the filing of the bankruptcy petition. It did so, however, on the ground that the original loan was a *joint* one made by both the SBA and a private lender, with federal funds disbursed at the time of the underlying loan, prior to bankruptcy.[43] While the SBA lacked legal title to the note prior to the assignment, "beneficial ownership of the three-fourths of the debt for which priority is asserted belonged to the Administration from the date of the loan." 364 U.S. at 450. No such beneficial ownership is present here, since no federal funds were advanced prior to February 3, 1971.

The *Eklund* decision is also distinguishable on several grounds. First, as in *McClellan*, *Eklund* involved a loan in which the SBA disbursed funds and held a participation interest, rather than simply guarantying a secured creditor. 369 F. Supp. at 1054. Second, that case involved mechanics' liens entitled to a superpriority under state law, rather than security interests whose ordinary priority was determined at the time of their perfection. 369 F. Supp. at 1055. If the case had involved competing security interests perfected at the time of the filing of the mechanics' lien claims, the security

[43] *See Small Business Administration* v. *McClellan*, 272 F.2d 143, 144 (10th Cir. 1959), *rev'd*, 364 U.S. 446 (1960).

interests would have been second in time and therefore junior to the SBA under the U.C.C. Third, the district court seems to have concluded incorrectly that the mechanics' liens became choate when they were recorded. Since the liens probably were inchoate under *United States* v. *White Bear Brewing Co.*, 350 U.S. 1010 (1956) (*per curiam*), it was unnecessary to reach the relation back question (assuming the choateness doctrine was applicable at all[44]). Finally, to the extent that the language of the case suggests support for the government's "relation back" theory, it is directly contradicted by a more recent district court decision. *City of New York* v. *United States*, 414 F. Supp. 90 (E.D.N.Y. 1975).

The principle governing this case is to be found in *United States* v. *Marxen*, 307 U.S. 200 (1939), which was discussed and distinguished in the *McClellan* opinion. The facts in *Marxen* were not unlike those in *McClellan*, except that the federal agency there (the FHA) had merely insured a loan, similar to the SBA's guaranty here, rather than participating in it directly. The Court concluded that there was no debt due the United States at the time of bankruptcy, when the rights of creditors become fixed, and the government therefore was not entitled to priority by virtue of the post-bankruptcy assignment. 307 U.S. at 207.

In subsequent cases, relying upon *Marxen*, courts have consistently held that a security interest assigned to the federal government does not enjoy the special benefits available to federal lien claims as of a date prior to the assignment. *In re Miller*, 105 F.2d 926 (2d Cir. 1939); *Engleman* v. *Commodity Credit Corp.*, 107 F. Supp. 930 (S.D. Cal. 1952); *In re Wood's Estate*, 171 Misc. 542, 12 N.Y.S. 2d 816 (Surrogate's Ct. 1939). *See also Bulls* v. *United States*, 356 F.2d 619, 623 (5th Cir. 1966). Thus, in *United States* v. *Brocato*, 403 F.2d

[44]See note 26 *supra*.

105 (5th Cir. 1968), the court was confronted with a "Deferred Participation" agreement containing a clause which provided that the indebtedness was automatically transferred to the SBA upon the debtor's bankruptcy. The purpose of this provision was to circumvent the *Marxen* decision,[45] but the court refused to sanction this attempt to elevate form over substance. Relying on *Marxen* and *McClellan*, the court stated that for the insolvency priority statute to apply, the SBA must have had either legal title or beneficial ownership of the debt prior to the filing of the bankruptcy petition. In order to have beneficial ownership under *McClellan*, the court stated that "the SBA *must actually advance money* to the debtor prior to the filing of the bankruptcy petition." 403 F.2d at 105 (emphasis added). Since the SBA lacked legal title at that time, and there was "no prior 'beneficial ownership' to which a transfer could relate back", the insolvency statute was held to be inapplicable.

While these cases were concerned with the insolvency priority statute, which is not involved in this case, the principle which they enunciate is equally relevant here.[46] As a voluntary commercial assignee, the government is entitled to the rights possessed by its assignor. Under the insolvency priority statute and the related choate lien test, the government also enjoys some special benefits which are unavailable to other secured creditors in litigation.[47] The clear message of these cases arising under R.S. § 3466 is that the government cannot claim those benefits retroactively, as of a date when the government was not a secured creditor at all. There is

[45]*See* Comment, *The Relative Priority of Small Business Administration Liens: An Unreasonable Extension of Federal Preference?* 64 MICH.L.REV. 1107, 1111-12 n.32 (1966).

[46]The government, by citing *McClellan*, apparently recognizes the relevance of such cases.

[47]As has been described above, however, many of such benefits have been limited or abolished in recent years.

no reason why this should be any less true for the choate lien test than it is for the insolvency priority statute. In fact, there is substantially less justification for retroactivity in the case of the choateness doctrine, which is without statutory basis.

Nothing to the contrary is stated in the cases from some of the courts of appeals applying the choateness doctrine in order to subordinate statutory liens to federal consensual liens. In *Willow Creek Lumber Co.* v. *Porter County Plumbing & Heating, Inc.*, 572 F.2d 588, 590 (7th Cir. 1977), the court apparently recognized that choateness should be tested at the time the assignment was recorded. Referring to the mechanics' liens in that case, the court said:

> These liens were not reduced to judgment on January 2, 1975, the date when the assignment of the mortgage to the United States was recorded. Accordingly, if the federal priority rule applies, the lien of the mortgage is entitled to priority, and the judgment must be affirmed.

A secured party extending continuing credit pursuant to a future advance clause should be able to evaluate its relative priority position under the applicable state law, without having to speculate whether a junior security interest may someday be created and sold to the government and be catapulted to senior status through the retroactive application of the choateness doctrine. As the court of appeals stated in its opinion below, "[i]t was only when the SBA bought into the note in February 1971 that Kimbell could have actual notice of the existence of a federal lien and the application of federal law." 557 F.2d at 505. The application of the choateness doctrine to determine the relative priority of perfected security interests would seriously undermine the commercial certainty which is the foundation of the secured lending industry. The retroactive application of that doctrine would erode that certainty still further.

B. KIMBELL'S SECURITY INTEREST WAS CHOATE AT ALL RELEVANT TIMES.

Kimbell's security interest in O.K.'s property was created and perfected by the three security agreements executed and filed in 1966 and 1968. Thereafter, Kimbell held the senior security interest in that property, both before and after the secured loan by the Bank in 1969. At any point in time, Kimbell's security interest was fully choate under the principles developed by this Court; most particularly, that security interest was choate on February 3, 1971, when the SBA first acquired any interest in the Bank's security interest in the property.

As developed by this Court, the choate lien test merely requires that the identity of the lienor, the identity of the collateral, and the amount of the debt secured must be certain. *United States* v. *City of New Britain*, 347 U.S. at 84. Each of these elements was satisfied in the present case. Only the last element is contested by the government.

The government's sole challenge to the choateness of Kimbell's security interest relates to the third element of the choate lien test, concerning the certainty of the amount of the debt. Despite the government's contentions to the contrary, however, that element was satisfied. The amount which O.K. owed Kimbell changed from time to time, as O.K. made payments to Kimbell and Kimbell sold more inventory to O.K.[48] At any point in time, however, the amount of this contractual debt was fixed, certain, and liquidated in amount. For example, in February, 1969, when Republic made its loan to O.K., the debt was $18,390.93. From January 15, 1971 forward, the amount of the debt was fixed at $18,258.57, a few dollars less than it had been at the time of

[48] Similarly, the amount of the debt secured by the Bank's security interest changed, as interest accrued and payments were made.

the Republic loan. This is the exact amount of the principal claim for which Kimbell obtained judgment, plus interest and attorney's fees.[49]

The controlling case on this point is *Crest Finance*. The government has apparently misunderstood the facts in *Crest Finance*, arguing that it is distinguishable because there "the amount due was established by the face amount of the lienor's note."[50] That was not the fact or the issue in that case.[51] As the Solicitor General's office acknowledged in *Crest Finance*, when it confessed error on behalf of the government, the debtor there had executed not one but nine separate notes, and a substantial part of the aggregate principal amount of those notes had been repaid by the debtor in two lump-sum payments. Memorandum of the United States at 3, *Crest Finance Co.* v. *United States*, 368 U.S. 347 (1961). The amount due was the sum of all the advances and accrued interest evidenced by the notes, less the total amount repaid.

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[49]Reasonable attorney's fees covered by a perfected security interest also should be treated as choate, in the same manner as interest accruals. This Court's rulings in *United States* v. *Pioneer American Ins. Co.*, 374 U.S. 84 (1963) and *United States* v. *Equitable Life Assurance Soc'y of the United States*, 384 U.S. 323 (1966) holding such fees inchoate in a federal tax lien priority contest were superseded by the 1966 Federal Tax Lien Act, 26 U.S.C. § 6323 *et seq.* (1976). Among other things, those amendments provided that attorney's fees incurred in enforcing a lien or security interest which has priority shall enjoy that same priority, despite the fact that they might be characterized as inchoate. 26 U.S.C. § 6323(e)(3) (1976).

[50]Petitioner's Brief at 55 n.60. *See also id.* at 42 n.48. Even in a situation where a debt is represented by a single note or bookkeeping entry, there will be factors which will affect the actual amount owed, such as periodic payments, set-offs, subsequent oral modifications, interest accruals, disputes over interpretations of terms, and the like.

[51]The Conference appeared as *amicus curiae* in the *Crest Finance* case in this Court and before the court of appeals.

The amount of the indebtedness, although fixed and certain, could not be ascertained from the notes in *Crest Finance* any more than from the notes in this case. The amount owed Kimbell by O.K. was the sum of the sales to O.K. less payments made by O.K. That amount was every bit as certain as the debt in *Crest Finance* and was determined in exactly the same manner—from the books and records of the parties.

The position taken by the government in its brief on the standard of choateness, and its reliance upon *United States* v. *R. F. Ball Construction Co.*, 355 U.S. 587 (1958),[52] is completely inconsistent with its position in *Crest Finance*, where it confessed error. In distinguishing the *Ball Construction* case, the Solicitor General stated:

> The issue [in *Ball Construction*] was whether an open-ended assignment, purporting to secure future contingent liabilities, was effective to give the assignee priority for *an indebtedness that did not come into existence until after the federal tax lien arose and was recorded*. This Court properly held that it did not, but that decision is in no way dispositive of this case, for here the indebtedness secured by the lien arose from advances made contemporaneously with the assignments. *The difference between this case and* Ball, *in short, is that at the time the tax lien arose the indebtedness secured by the competing lien was, in* Ball, *not yet in existence and, in this case, fully liquidated.*

Memorandum for the United States at 7, *Crest Finance Co.* v. *United States*, 368 U.S. 347 (1961) (emphasis added).

In contending that O.K.'s debt to Kimbell was not sufficiently certain in January, 1971, the government relies on the argument that the amount of a debt cannot be certain until it is reduced to judgment or enforceable by summary proceedings, in spite of the clear holding to the contrary in

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[52]Petitioner's Brief at 53.

Crest Finance.[53] It is clear that no judgment is required to make a fixed contractual debt of this kind certain in amount, as distinguished from a statutory lien securing an unliquidated debt. The government's theory is yet another example of the kind of confusion which has been engendered by the choateness concept.

None of the cases cited by the government (Petitioner's Brief at 54–55) suggest that a judgment is necessary to establish certainty for purposes of the choateness test, particularly for a contractual debt. *See Crest Finance. New Britain* simply states the general requirement of certainty, and despite the fact that the state and local tax liens involved there had not been reduced to judgment, the Court remanded the case for a determination of their choateness. *United States* v. *White Bear Brewing Co.*,[54] *United States* v.

[53]Since the government's first claim as a secured creditor arose on February 3, 1971, after the last shipment of goods to O.K. from Kimbell, this case does not involve the viability of either future advance clauses or after-acquired property clauses under the choateness doctrine. Such clauses are fully authorized by the Code and have been for many years a common and accepted part of modern commercial financing practice. Powerful reasons of logic and established commercial practice exist for treating the debt and collateral covered by such clauses in the same manner as the initial debt and collateral, for purposes of the choate lien test. Even in the bankruptcy preference context, where the courts have limited flexibility because they are interpreting statutes rather than formulating judicial rules, interests in after-acquired collateral arising during the preference period of Section 60 of the Bankruptcy Act have been treated as perfected as of the initial date of perfection of the security interests in question. *See, e.g., In re King-Porter Co.*, 446 F.2d 722 (5th Cir. 1971); *DuBay* v. *Williams*, 417 F.2d 1277 (9th Cir. 1969); *Grain Merchants of Indiana, Inc.* v. *Union Bank & Sav. Co.*, 408 F.2d 209 (7th Cir.), *cert. denied sub nom. France* v. *Union Bank & Sav. Co.*, 396 U.S. 827 (1969). The same result is embodied in Section 547 of the Bankruptcy Act of 1978, which is awaiting the President's signature. After acquired security interests in accounts and inventory are protected as long as the secured party does not improve its position at the expense of the estate.

[54]350 U.S. 1010 (1956).

Vorreiter,[55] and *United States* v. *Col[illegible]a*,[56] were all *per curiam* reversals which did not state the basis for the decisions, so that it is unclear what the fatal flaw was in those cases. Furthermore, all three cases involved competitions between federal tax liens and mechanics' liens, rather than between contractual U.C.C. security interests. While the amount actually recoverable under a state-created mechanic's lien may often be unliquidated or the subject of dispute and the vagaries of state law, no such uncertainty exists with a U.C.C. security interest in a contractual commercial credit setting, such as is involved here. Accordingly, there is nothing in those cases to suggest that Kimbell's claim had to be reduced to judgment in order for it to be certain.

In both *United States* v. *Pioneer American Insurance Co.*, 374 U.S. 84 (1963) and *United States* v. *Equitable Life Assurance Society of the United States*, 384 U.S. 323 (1966), the government conceded the choateness and seniority of prior perfected real estate mortgages which had not been reduced to judgment. The government contested only the choateness of the attorneys' fees in those cases. Similarly, in *Crest Finance* the government conceded and this Court held that the unpaid balance of a series of secured loans was choate, despite the fact that the amount was not reduced to judgment prior to the filing of the notice of tax lien.

There is simply no requirement under the choate lien test that a contractual obligation, liquidated in amount, must be reduced to judgment in order for the security interest which secures it to be deemed choate. If adopted by this Court, the government's proposition that a judgment is necessary to make this secured debt certain and choate would mean that there is no such thing as a choate security interest, and that virtually the only possible choate lien is a judgment lien.

[55]355 U.S. 15 (1957).

[56]350 U.S. 808 (1955).

CONCLUSION

Programs of financial aid to businesses, funded by the federal government and administered by its agencies, have grown rapidly in recent decades. These programs supplement the amount of credit otherwise available to these businesses, and are reflections of public policy decisions to support particular segments of commerce in this country.

The role of the government agencies in these programs is the same as private commercial creditors, with discretion concerning when and on what terms to extend credit. In that sense, the traditional conception of the government's sovereign function as an involuntary creditor seeking to collect claims for unpaid taxes is not a useful basis for resolving questions of priority between voluntary federal commercial secured claims and secured claims of other commercial lenders.

The Conference does not question the policies underlying such federal programs or seek any advantage for private secured lenders in priority contests with agencies administering such programs. The Conference asks only that the well understood, comprehensive and fair priority rules of Article 9 of the U.C.C., upon which the entire commercial financing industry relies, not be made meaningless by extending the choate lien test beyond its statutory basis.

Public notoriety by filing, or comparable means to prevent deception, are at the heart of the perfection and priority concepts of the Code. If the government prevails here, reasonable expectations as to the priority of perfected security interests of the banking and commercial segments of this country, based on their reliance upon public filing or other antideceptive rules, would be destroyed by granting special superpriority status to subsequent federal secured claims. Except for pure speculation, no basis would exist for knowing whether or when federal credit might be extended and

become retroactively senior to existing secured interests. There is no practical method of protecting existing investments under these circumstances.

The choate lien test, whatever its strengths and weaknesses in other contexts, has no place in the resolution of priorities among perfected security interests arising under the Uniform Commercial Code, even those granted to or purchased by the government. The Congress recognized this in the tax lien area in 1966, when it responded to heavy criticism of the choateness doctrine by virtually abolishing the choate lien test as applied to perfected security interests.

The formula which puts all secured lenders on an equal footing and facilitates their business planning is that which is embodied in the Code. The Code represents a national law of commerce, and has received explicit recognition from Congress by its adoption of the Code for the District of Columbia and its protection of Code security interests in the Federal Tax Lien Act of 1966. It is to perfection under the U.C.C., rather than the choate lien test, that this Court should look to determine the relative priority of security interests. Accordingly, the judgment of the court of appeals should be affirmed.

Respectfully submitted.

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